QUEST

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QUARTERLY REPORT
JUNE 2011

John Citizen Family Superfund

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Mr John Citizen

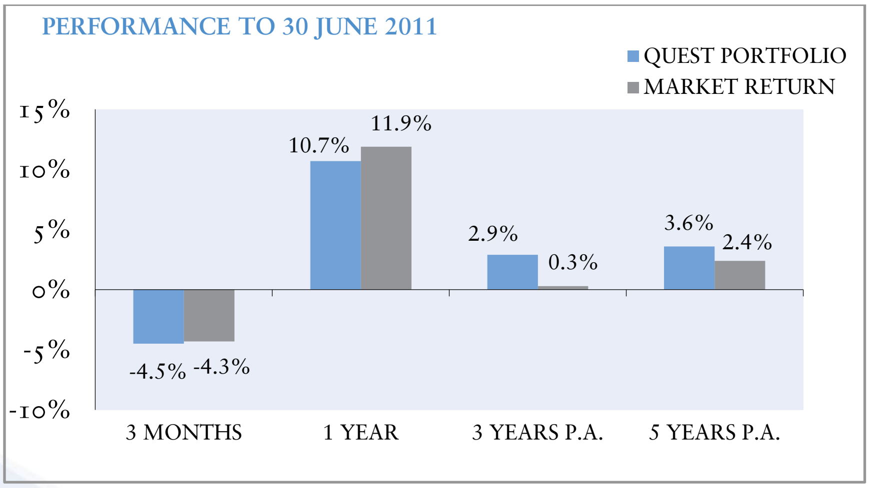
123 ABC Street
Sydney NSW

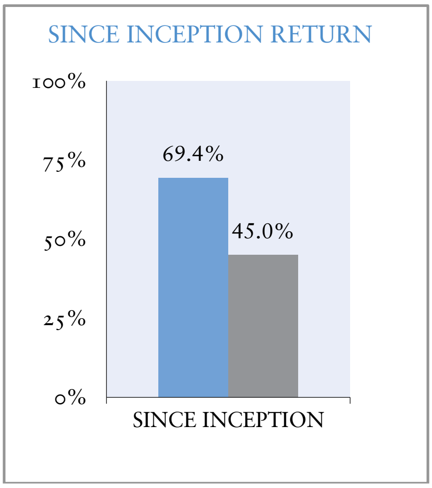
Account Name: John Citizen Family Superfund

PORTFOLIO MOVEMENT – 30 JUNE 2011	
PREVIOUS MARKET VALUE 31 MARCH 2011	
CONTRIBUTIONS DURING QUARTER	
PORTFOLIO MOVEMENT*	
MARKET VALUE «END_OF_PERIOD»	

YOUR PORTFOLIO PERFORMANCE FOR THE QUARTER*	
MARKET RETURN (S&P / ASX 300 ACCUMULATION INDEX)	

*Includes any fees for the quarter





** The portfolio returns quoted above represent the return achieved if invested in the Quest portfolio since inception (February 2005). Individual returns will differ for investors that made an initial investment after this inception date or where additional investments or redemptions have been made. Quest returns are net of fees. Past performance is not a reliable indicator of future performance.

MARKET SUMMARY

A VOLATILE QUARTER SAW THE MARKET PULL BACK SEVERELY IN MAY AND JUNE BEFORE RECOVERING. THE AUSTRALIAN DOLLAR HIT A HIGH OF $1.09 AGAINST THE US DOLLAR. THE US ECONOMIC RECOVERY LOOKS TO BE FAULTERING WHILE GREEK DEBT AND FUNDING DOMINATED THE ECONOMIC NEWS. A 10% MARKET CORRECTION PROVIDED QUEST WITH MANY OPPORTUNITIES AT GOOD PRICES FOR LONGER TERM INVESTORS.

The June quarter was burdened by negative international economic issues and a very strong Australian dollar. While the quarter started well, mid April saw the market pull back 10.5% over nine weeks before a rally in the last week of June. The market fell in each of the three months of the quarter and the ASX Accumulation finished down 4.3% for the period. The Quest portfolio posted a similar return to the market for the quarter.

During the quarter, the best stock performers included Telecom New Zealand, the defensive utility stocks Envestra, MAp Group and Spark Infrastructure. Mineral sands player Iluka Resources rose 36% while demerged beer producer Foster's Group popped 12%.

The laggard sectors were energy, consumer discretionary and materials. The worst energy performer was Woodside Petroleum which announced further project delays on the Pluto 1 gas project in Western Australia. The consumer discretionary sector continued to perform badly as retail shoppers prefer to save than spend. Myer was down 20% and Billabong down 25%. The materials sector, which is a mixed bag of stocks dominated by resources, reflected the mood of the quarter with Gunns Limited down 77%, Bluescope Steel down 44%, Leighton down 34% and One Steel down 23%. Fairfax fell another 28%. Quest did not own any of these stocks during the quarter.

The Small Companies index fell 5% over the quarter but within that result was a broad range of outcomes. Hastie Group shares collapsed from 80 cents to 14 cents, Pharmaxis failed to deliver satisfactory trial results and toppled from $2.50 to $1. A gaggle of stocks fell 50% or more: Berkeley Resources, Paperlinx, Brockman Resources, Customers Limited and more. Small cap winners included recoveries in stocks that lost a lot of ground in the previous quarter: Sigma Pharmaceuticals, Programmed Maintenance and Spotless. Telecom New Zealand was up 25% after joining the small stock index and finalising fibre roll out details in New Zealand. Index inclusion continues to create disturbing price distortions, particularly in small cap stocks.

Resources action was dominated by cost blow outs on major projects. Woodside announced further cost increases of $900m and a delay in the production of gas from the Pluto project until March 2012. The Pluto budget is now a whopping $14.9 billion. Gindalbie Metals confirmed an increase in the development cost of their Western Australian magnetite project of $700m to $2.67 billion. BHP announced the expansion cost of the Worsley alumina refinery in Western Australia was up by $1 billion to $2.9 billion.

These costs increases are mainly due to input costs; concrete and steel. Labour is a factor but more due to an increase in budgeted hours than wage pressures. Wage pressures are very real but less significant in such large projects. The size of development projects on the drawing board suggests that Australia lacks both the workforce and the capability to deliver so much in a short time. There are dozens of other projects, including the NBN, experiencing the same pressure. Queensland alone is approaching $70 billion in construction on Gladstone LNG projects of which two have reached Final Investment Decision. These projects are not all deliverable in our view.

Equinox Minerals was bid for by Canadian gold giant Barrick Canada in April for C$8.15. This occurred only a few months after Equinox bid for Citadel Resources, a major stock in our Quest portfolio. Equinox was delisted on 1 July 2011.

The government blocked the ASX take over by Singapore Stock Exchange in April. We were relieved to see this outcome, not because we did not own ASX but because we fail to see the benefit to Australia from selling our national stock exchange.

The Federal budget came and went in May. Like most budgets, the flurry of news died quickly with the severity of the actual outcome falling well short of the dire warnings that preceded it.

Returns from the various markets and indices for both the quarter and the twelve months to the end of June 2011 are summarised in the table below.

INDEX	**JUNE 2011 QUARTER**	**FISCAL YEAR 2011**
Dow Jones	0.8%	27%
S&P 500	-0.4%	28%
Japan Nikkei	0.6%	4.6%
ASX 300 (accum.)	**-4.3%**	**12%**
ASX Industrials	-6.1%	11%
ASX Energy	-11.1%	7%
ASX Financials	-4.6%	3.5%
ASX Small Companies	-9.7%	26%
ASX Materials	-5.5%	17%
A$ v US$	4%	27%
Oil	-10.6%	26%
Gold	4.7%	20.8%

Source: Iress

Corporate activity included the spin off by Fosters of their wine business, now known as Treasury Wine Estates (TWE). The beer business retained the old Foster's name.

Tabcorp also spun off the casino business, Echo Entertainment, in an attempt to create greater value for shareholders. The Tabcorp entity retains wagering and gaming while Echo owns the Sydney Casino, Jupiters Gold Coast, Treasury Brisbane and Jupiters Townsville. We did not participate in either of these attempts to release value, but it is interesting to measure the end result of the demergers.

A Foster's share bought on 1 April 2011 when the demerger was expected but not approved by shareholders would have cost $5.75. That share is now worth $6.20 after adding the Foster's current price to the TWE shares received on a 1 for 3 basis. That return includes the rejected bid for Foster's by SAB Miller at $4.90 and speculation that TWE could be taken over; but it is still a gain. It seems the Directors of Foster's have successfully released value for shareholders but only by attracting a take over bid.

Now for the Tabcorp demerger. At the same date of 1 April 2011 Tabcorp was about $7.45. The share is now demerged and trading at $3.20. Adding the Echo share at $4.20 today gives $7.40. Not much difference, a nil sum game here.

Earlier in the year the Westfield Group demerging of Australian operations gave a similar result. After spending $240m on the demerger, the market did not consider the sum of the parts to be more than the whole.

Our conclusion is that this is a good result; if sudden revaluations of demerged assets did result, it would reflect poorly on market analysis. If the objective is to create an asset that is more likely to be taken over; then so be it. It seems to have worked for Foster's but we are not convinced that buying into a demerging event for the sake of the event makes much sense for our investors.

In May, Spotless Group rejected a private equity proposal to take over the company at $2.50. The announcement provided a rare moment of excitement for Spotless shareholders who have successfully missed the last two stock market booms. Spotless has been a stock for the very, very, very patient investor for a decade now.

Finally, the saga of Greece and the associated economic mess drags on. Greece has a population of only 11.2 million according to Wikipedia. On a per head basis they have created an extraordinary level of global angst by feeding an increasingly dysfunctional economy with foreign debt over a few decades. We can't just blame the Greeks however, as Eurozone leaders have approved another 110 billion Euro in loans essentially to cover all the previous loans made by mainly European banks. The Greek rescue is an exercise in buying time; the austerity program is as severe as it is dangerous. The loan package defers the need for European banks to take a loss, an option that is seen to be politically unpalatable. Surely someday the buyers of risk assets will be held accountable for the risk they take on.

The austerity program will put huge pressure on consumers as jobs are lost and consumption falls. If the effects are severe, it will be the Greek banks that have loan exposures to the population that feel the pressure as borrowers default. The pressure will spread from foreign banks into the local banks. The only thing that is certain here is that this issue will be back to haunt us again. Similarly, it is possible that Spain, Ireland and Portugal also disturb markets in the coming months.

PORTFOLIO ACTIVITY

SOME LARGER STOCKS WERE REPLACED BY SMALLER STOCKS AS THE MARKET FELL 10% DURING THE QUARTER. BANKS, THE BEST SOURCE OF FRANKED YIELD IN THE MARKET, WERE BUILT UP TO 28% OF THE PORTFOLIO. EQUINOX WAS TAKEN OVER BY BARRICK MINING OF CANADA.

During the quarter, four new stocks were added to the portfolio: Sundance Resources, Swick Mining, Transfield Services and Wesfarmers. These were funded by cash and sales of GPT Group, Incitec Pivot, Ten Network and Westfield Group.

Sundance Resources is developing the Mbalam Iron Ore project in southern Cameroon and northern Congo. The area is seen as an emerging iron ore province requiring significant development of port and rail infrastructure. Our interest is spurred by the potential for a partnership to be developed, possibly seeing a sell down by Sundance in exchange for cash that will fund a reduced share of the overall project. The company has announced that discussions are underway at present. The Sundance team have pushed on with the project despite tragically losing the entire board in a plane crash in Cameroon in 2010. The JORC resource of 484 mT 61% Fe is located 510 km from the proposed port of Lolabe on the west coast of Cameroon.

Swick Mining provides underground diamond drilling services to mining companies in Australia and North America. While rated a “C” grade stock under our process, strong demand for drilling rigs from mining companies is increasing utilisation rates for Swick and new contracts are being struck on improved terms. This suggests strong earnings growth and on our valuation the company is good value.

While we are positive on the outlook for miners in general, the persistent budget pressures and high capital commitments of the miners make the service providers a sensible alternative.

The same theme led us to the investment in Transfield in April. Transfield has had a lacklustre performance over the last five years due to poor management and debt problems in the GFC. New management has overseen the acquisition of Queensland driller Easternwell, a stronger balance sheet and disposal of poorly performing US businesses. With this, Transfield faces a brighter outlook and should begin to post much improved earnings. Transfield trades below our valuation and we expect it to re-rate as earnings improve. The company’s core business is facilities maintenance and engineering services with clients such as BHP, Caltex, Woodside, Australian Rail and Track Corporation and is also involved in the initial NBN roll out in Kiama south of Sydney.

Wesfarmers was added to the portfolio in June. The diversified owner of coal mines, Coles, Target, K Mart and Bunnings is our only retail exposure. Something of a market favourite, the stock finally reached a reasonable price level under our process. Wesfarmers also has bolstered our Top 20 portfolio exposure which was even lower than normal after our selling of Westfield and News Corporation.

GPT Group was sold as our price target was reached. We bought this position when Stockland sold their “strategic” holding last November at

$2.75. We bagged a good return here selling at around $3.16 plus 9 cents in distributions.

Incitec Pivot was sold as we reviewed our position on this stock. We bought this as a short term investment late last year. With hindsight we should have taken profits in March when our price target was nearly achieved. In the end, entry and exit prices were similar resulting in a small net gain. Westfield was sold as we considered the near term growth prospects to be uninspiring compared to other investment opportunities. Ten Network was a poor investment and has been sold.

The 10.5% correction during May and June saw additional shares added to our positions in BHP, Orica, RIO, Westpac and ANZ. The Quest bank holdings are nearly 30% of the portfolio and the highest bank exposure we have owned to date. We are attracted by the high sustainable dividend yield despite global economic concerns. We think the banks were sold too heavily in May.

BHP was the most significant move with a major reduction in the position occurring in the heady days of the buy back in April. The announcement of the buy back pushed the stock beyond $47. Quest did not accept the buy back on behalf of our clients due to the diverse range of structures and tax rates amongst our client base but we took advantage of these prices by selling into the market. The stock made a rapid descent back to $42 where we rebuilt the position.

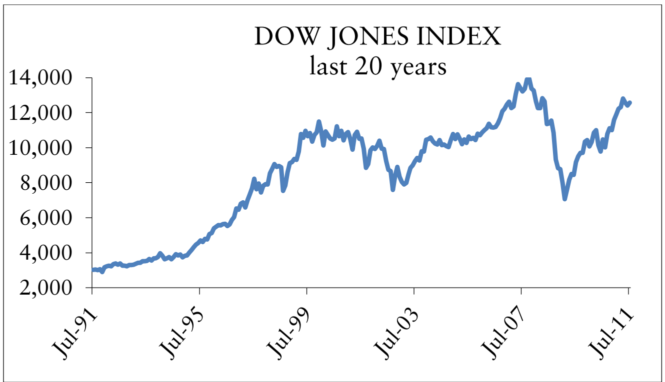
Citadel has been an excellent investment for Quest. Equinox bid for Citadel in December 2010 resulting in Quest then holding Equinox shares. Equinox is a copper producer listed in Australia and Canada. Quest then received a bid for our Equinox holding from Minmetals in April 2011 and a further bid from Barrick Canada at Canadian $8.15. We sold the stock in the market to avoid the settlement delay of a Canadian bid at around $7.90 in May. Barrick now owns more than 90% of Equinox.

The return to our early investors from holding Citadel from October 2008 was about 275%. Equinox (formerly Citadel) was the seventh stock held by Quest to receive a take over bid (six of which succeeded) since the inception of Quest in 2004.

OUTLOOK

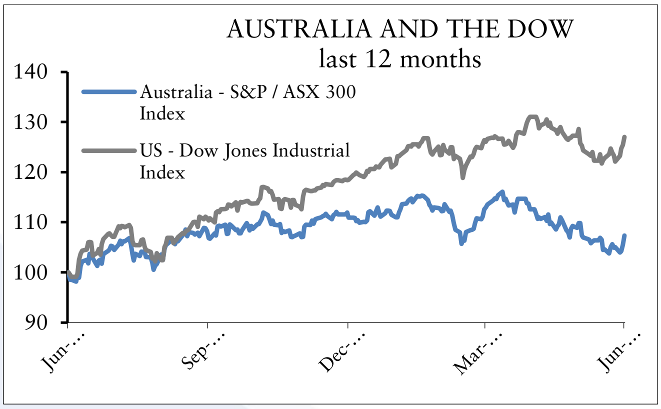
MARKETS HAVE ENDURED NATURAL DISASTERS, ESCALATING SOVEREIGN DEBT CONCERNS AND THE PERCEPTION OF SLOWING GROWTH IN THE US AND CHINA. THE AUSTRALIAN STOCK MARKET HAS FARED WORSE THAN MOST AND IS NOW SHOWING GOOD VALUE. DESPITE LINGERING CONCERNS, A MARKET RECOVERY IS ON THE CARDS.

Despite the precarious state of the US budget, high US unemployment, the woeful state of the US housing market and a tumbling US dollar, the US Dow Jones is approaching post GFC (and all time) highs as seen in the chart of the last 20 years below.



Source: Iress

The Australian market has severely under performed the US market, despite our booming resource sector and relatively stronger economic position. This decoupling worsened in the last 12 months and is starkly shown in the chart below.



Source: Iress

Australia navigated the GFC well thanks to an economically prosperous ten years leading up to 2008. On most macro measures, the economy remains strong. Unemployment is low and thanks to the resource boom our terms are of trade are at record levels. Interest rates have normalised, government stimulus has been withdrawn from the economy and our position is envied by many. So where is the problem?

The Australian dollar is very high, making our shares expensive. Interest rates are high; it is easy to leave money in the bank at attractive rates. Consumer confidence is low, residential housing prices are slipping and investment confidence is poor. Government is compromised by a tenuous majority and is creating an atmosphere of uncertainty.

In contrast, the USA still has very low interest rates and ongoing government stimulus has ensured liquidity remains high and money cheap. This excess liquidity has driven up asset prices including shares, bonds and many commodities. The US dollar has tumbled because there are so many US dollars available! Given this, the US Federal Reserve called to a close their second round of "quantitative easing" (QEII) at the end of June.

Australia is wrestling with a reliance on China to keep the resource music going and a parliament that may not go the distance. High commodity prices have pushed up the Australian dollar and are causing problems in many non-resource sectors. Education, tourism, manufacturing, building and retailing, large employers of everyday Australians, are all suffering.

The knock-on effect to consumer sentiment and demand for credit has been marked with both at depressed levels. Forecasts for domestic GDP have progressively been wound back, even after accounting for the flurry of natural disasters of the last 12 months.

Having hiked rates from the 3.0% low in 2009 to the current 4.75% in November 2010, the Reserve Bank of Australia now faces a dilemma. Publicly they maintain the stance that further rate rises may be needed to manage the effects of the bolus of business investment coming down the line. The subdued economic data of recent weeks is now causing a rethink.

Markets were pricing another 0.25% to 0.5% rise in rates this calendar year but it seems likely to us that rates will now remain steady. The fact is that financial conditions, a measure which includes the combined impact of interest rates, currency, yield curves, corporate bond spreads and equity market returns, are very tight. This is made worse at the consumer level by higher utility prices, new taxes and a growing lack of faith in our political decision makers.

We also remain sceptical about the deliverability of the enormous list of projects in the pipeline. The economy has a narrow base and is vulnerable to being thrown off balance if things don't play out as the RBA expect. We would not be surprised to see a shift to lower interest rates later in the year.

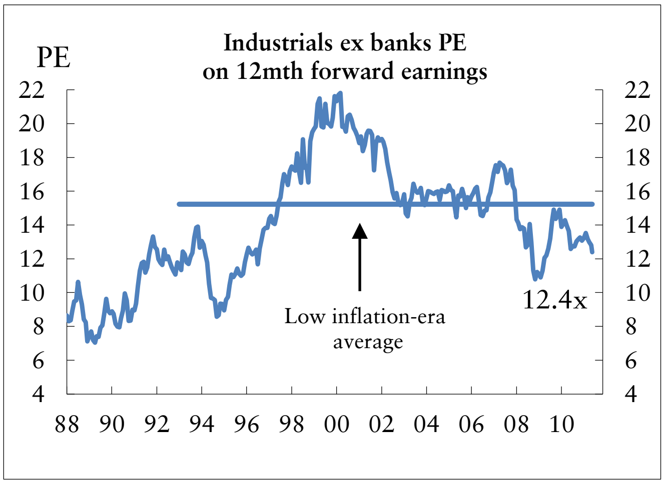
This would be a very significant development. The prospect of lower rates would see the Australian dollar fall and some of the most beaten up Australian industrial stocks come to life. Retail and building stocks stand out. Also, stocks with offshore earnings could quickly make up for lost time.

The good news is that Australia has plenty of ammunition to bat back an economic challenge, with interest rates amongst the highest in the world. It is also easy to forget that equity markets do not behave the same way as the underlying economy. Markets react much earlier in anticipation of future changes in the economy rather than to the changes themselves.

Valuations currently look attractive and we took advantage of some opportunities to invest when the market fell apart in April and May. Despite the market rebounding 3-4% since the lows of June, your average domestic industrial stocks (typically a cyclical stock) look very cheap compared to defensives. On a medium-term view, banks also look attractive providing a reliable full franked yield of over 7%.

Experience has shown that our Quest company valuations have proven to be a good guide to market value over time. There are periods when we struggle to find stocks trading below our bottom-up valuations for individual companies. More often than not, the market then proves to be expensive and doesn't perform well. The reverse also holds; when many stocks trade below our valuations we often see the market rally shortly after. At present we have no trouble finding stocks trading below our valuations. Either the outlook built into our forecasts is optimistic or value exists today. We think the latter given we are typically conservative in our forecasting.

Brokers however still have lofty forecasts built in for 2012 and we think these will come down. Revisions are likely to occur after reporting season in August. To some extent this is priced in with Australian industrial stocks now trading well below historical averages and as cheaply as they have since the recovery from the GFC.



Source: Deutsche Bank

Looking more broadly, the European fiscal situation remains unsettled. We can't see any easy way to untangle Greece, and perhaps the other fiscally destitute European countries, from the EU without real pain. A debt restructuring or a partial reconfiguration of the Euro seems inevitable. The latest bail out for Greece shows that political necessity will always take precedence over rationality and the problems will be put off for another day. Despite the hollow nature of these fiscal "fixes", markets tend to rally on such news as the extreme fear that was priced into markets rebounds. We expect this relief rally to continue in the near term.

The same logic can be applied to the equally challenged US economy. Recent economic data has been poor showing the recovery is lacking conviction. The fiscal imbalances remain. Despite this, the US market continues to perform. Absent another crisis, we expect the US to continue to muddle along ignoring the elephant in the room that is the US government debt. The economy may well worsen from here but the US Government and the Federal Reserve have a proven track record of doing whatever it takes to support the economy and asset prices. It may not take the form of QEII, given the political challenges Obama faces heading towards another election, there are other forms of stimulus likely if the recovery falters.

There is increasing concern in the market that China is slowing. Commodity prices are looking softer at high levels, particularly the bulk commodities. We are not convinced that there is significant downside and think some Australian resource stocks look to be reasonable value. We are wary of the market noise but also realistic about the momentum built into the enormous Chinese economy. After all, China has a population of 1.3 billion! BHP and RIO do not look expensive and a selection of smaller resource plays are still the subject of our analysis.

Overall, the Australian market looks to offer value. The question is how soon that value is likely to be realised. With a band aid now applied to the Greek crisis and noises from government officials in China appearing to suggest financial conditions might ease later in the year, global markets are likely to take a more optimistic stance. It remains to be seen if Australia joins in and how well the local Government negotiates its way through the rest of the year.

Share prices now look cheap and the economy has a number of buffers. We see reasonable prospects for sensible returns from well selected investments.

Should the market improve significantly, we will sell when target prices are reached. Should that occur, expect to see a build up of cash in the portfolio, perhaps to significant levels, as we await further investment opportunities to present themselves.

FEES

There is no performance fee payable this quarter.

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