QUEST

QUARTERLY REPORT
JUNE 2010

John Citizen Family Superfund

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Mr John Citizen

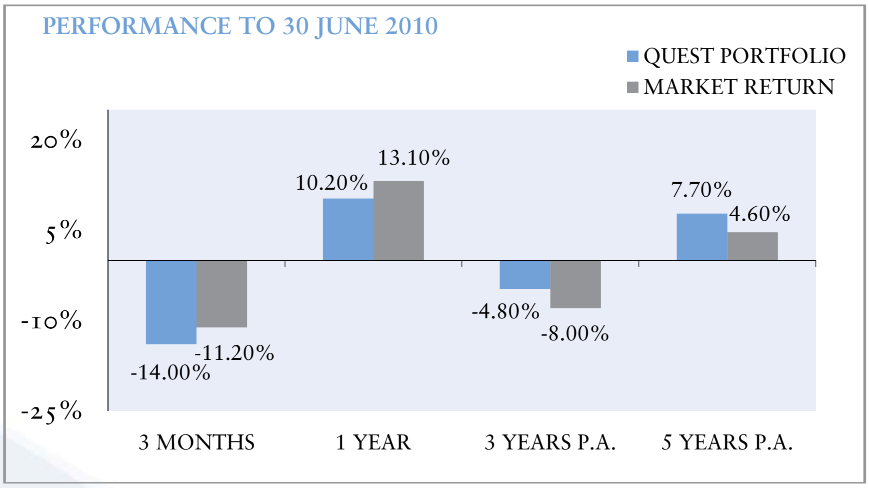
123 ABC Street
Sydney NSW 2000

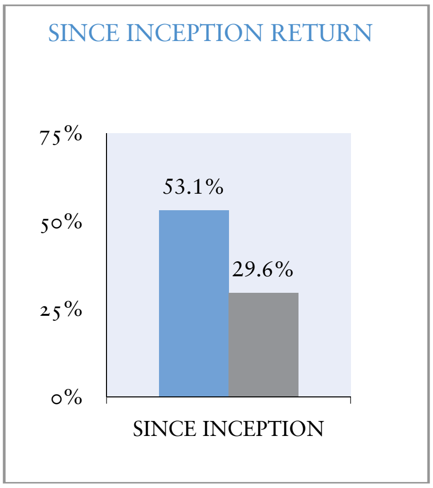
Account Name: John Citizen Family Superfund

PORTFOLIO MOVEMENT – 30 JUNE 2010	
PREVIOUS MARKET VALUE 31-MAR-10	
CONTRIBUTIONS DURING QUARTER	
PORTFOLIO MOVEMENT*	
MARKET VALUE 30-JUN-10	

YOUR PORTFOLIO PERFORMANCE FOR THE QUARTER*	
MARKET RETURN (S&P / ASX 300 ACCUMULATION INDEX)	-11.20%

*Includes 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

GLOBAL MARKETS LOST CONFIDENCE DURING THE JUNE QUARTER AS THE ECONOMIC OUTLOOK IN BOTH EUROPE AND THE US DETERIORATED. DATA POINTS HAVE BEEN MOSTLY POOR, LEADING TO A RUSH TOWARD CONSERVATIVE, DEFENSIVE STOCKS.

The June quarter was weak after the market peaked in mid April. The local market fell 11%, the Dow Jones fell 10%, the London FTSE 13% while Shanghai tumbled 23%.

Market sentiment was very negative in the last two months as investors fled from perceived riskier situations into defensive stocks. The concern globally is once again related to debt issues in both Europe and the USA that has led to European budget cuts and austerity programs that will make growth hard to find. In contrast to the global weakness, some smaller Asian markets such as Korea, Indonesia and the Philippines were flat or slightly higher over the quarter, with a perception that growth lies in the developing regions rather than in western economies.

In recent months the Chinese government changed the rules in relation to the construction industry, a major consumer of steel. The aim was to slow the construction of speculative apartments in favour of more affordable housing for the masses. Other initiatives were also enacted to slow a rampaging economy back to a more sustainable level. The markets reacted accordingly, with iron ore prices down 31% from the highs of April.

China had been growing at a massive pace with imports of raw materials being turned into metal and power to fuel the ongoing build in infrastructure and construction. The perceived slow down is a relative argument as Chinese growth will still run at 8% or higher for some years, albeit down from the recent 11% rate. This compares to an Australian growth rate of about 3% and the USA of around 2%.

Lower growth means lower global demand for metals which is not likely to be good for Australia. In this scenario, our currency deflates (the dollar fell from US$0.91 cents to US$0.84 during the quarter) and there is reduced international interest in our stock market.

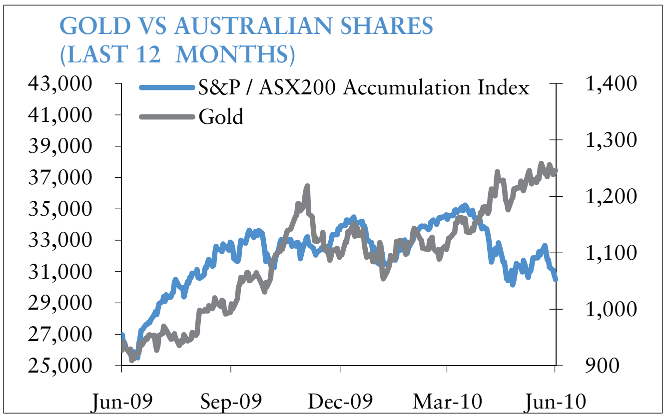
With commodity prices falling, resource stocks traded significantly lower during the quarter. Banks were also hit hard with Westpac down from $28 to $21 and CBA trading from $56 to $49.

These are big falls and suggest that offshore investors have taken profits on both the share price and the currency in recent months. The reasons are threefold:

1. a perception that the Australian dollar would ease with lower metal prices;
2. global concerns about debt levels have led to selling of financial stocks globally, and
3. fears that the sudden and unexpected tax changes made by the Rudd government would make Australia a riskier investment proposition. Recently, this was partially addressed.

Industrial stocks have also fallen. The reasons vary but it is true to say that the more conservative and less exciting stocks such as Amcor, Fosters and some property stocks did better than most. Stocks that are oriented to delivering strong earnings growth or exposure to a cyclical upswing clearly suffered, falling more than the index in most cases. That has been seen in stocks such as ASX ($34 to $29), Macquarie Group ($47 to $37), mid-size travel business Wotif ($7.40 to $5.40) and Seek ($8.50 to $7.00).

Given the global market concerns, gold continued to trade higher. Over the course of the financial year gold returned 29% versus 12% for the Australian market.



Corporate action continued during the quarter with Telstra ending the war with the government by selling core assets to the National Broadband Network for $11 billion. MacArthur Coal rejected three take over proposals in quick succession and both Sigma Pharmaceutical and Healthscope received take over proposals. Valemus (comprising Abigroup and Baulderstone) prepared to IPO at a market cap of $1.3 billion. This was subsequently abandoned in July due to the state of the market - an ominous sign for any IPOs planned for the near future.

PORTFOLIO ACTIVITY

WE SIGNIFICANTLY REDUCED OUR HOLDINGS IN RESOURCE STOCKS IN THE QUARTER IN ANTICIPATION OF MOVES BY CHINA TO SLOW ITS GROWTH. HOWEVER, CONCERNS ABOUT THE RISK OF EUROPEAN SOVEREIGN DEFAULT AND TEPID DATA FROM THE US KNOCKED THE MARKET DOWN SIGNIFICANTLY WITH ONLY DEFENSIVE STOCKS PUTTING UP ANY RESISTANCE. OUR PORTFOLIO STRUGGLED IN THIS ENVIRONMENT, POSTING A DISAPPOINTING PERFORMANCE.

Our expectation was that 2010 would see ongoing volatility with share prices alternating between optimism (as the global recovery takes hold) and pessimism (as financial risk increases with continuing high debt levels). The quarter provided both of these extremes.

Following visits by Chris Cahill to China / Mongolia and Michael Evans to the US, the portfolio was tilted for a period of slowing growth in China and a continuing recovery in the US. As a result, we significantly reduced our resource exposures, selling some of our BHP holding and exiting RIO, Alumina and Aquarius Platinum. We also added News Corp and Simsmetal and increased our holdings in CSL and Worley.

Whilst we called the fall in resource prices correctly, our portfolio didn't fully benefit given the high levels of pessimism that gripped global equity markets during the quarter. The market became concerned by the triumvirate of heightened risk of European sovereign default, slowing growth in China and disappointing economic data in the US.

The Quest portfolio didn't perform well in this environment as defensive stocks significantly outperformed all others. For example, we held no property stocks which held up very well compared to the rest of the market. Our bank holdings were the most disappointing as they were caught in the sell off by international investors of large Australian stocks. Significant falls in a number of our smaller holdings, notably Bauxite Resources, Citadel Resources and Elders, also impacted our performance.

As expected, Citadel Resources raised equity during the quarter and we participated via our entitlement. The threat of this raising had been impacting the Citadel share price for some time and we previously sold some of our holding in anticipation of this weakness. With this raising, the company can now fund the development of its copper and gold assets in Saudi Arabia. Funds from the raising also allowed Citadel to purchase a greater share of its key Saudi project. This purchase was done at a discount and enhances the value of Citadel shares, which remain an attractive investment in our view.

Our investment in Bauxite Resources has been a disappointment. We were attracted to the company's large bauxite tenements close to established infrastructure and ports in south west WA. They had also completed encouraging trial shipments of high quality bauxite to customers in China. Despite the simplicity of bauxite mining in this region (the ore is only metres from the surface and can be dug up with simple equipment), the company has had difficulties obtaining the appropriate approvals and licences for mining. The CEO has now been replaced and the company continues to pursue its strategy with the support of its major Chinese shareholders. The delay and uncertainty has severely impacted the share price and we remain in close contact with the Board and management in monitoring the situation.

We exited Elders during the quarter, losing faith in the turnaround of the company's core business which was taking longer and proving more difficult than expected. We undertook this small investment knowing it carried significant risk along with the potential for high returns. In the end, we sold out at a loss preferring to recognise the mistake and have moved on to other investments.

We also trimmed positions in Newcrest, Seek and Fletcher Building early in the quarter as share prices approached our target valuations.

A new position was established in Transurban, the owner of toll roads in Australia (CityLink, M2, M7, M5 and the Eastern Distributor) and the USA. We participated in an equity raising to fund the purchase of the Lane Cove Tunnel and upgrades to the M2 and M5. This capital raising resulted in the withdrawal of a previous takeover proposal for Transurban and the sale of shares held by one of the bidders. We know Transurban management and the company ranks highly as an "A grade" in our qualitative screen. We currently judge it as good value and added to our holding throughout the quarter.

An earnings downgrade by Sonic Healthcare in May saw the shares fall from $13 to $10. We are former holders of Sonic, having exited at higher prices in the past. We know Sonic well and regard it as a high quality company, though the potential erosion of earnings from further regulatory change by Government does impact our valuation. We re-established a small position in Sonic at around $10 given the significant discount to our target price.

We also took up shares in Super Cheap Auto when they conducted a placement at $4.80 to fund the purchase of Ray's Outdoors. This is a well run retailer and we recently visited management and a number of sites in Brisbane.

The Ray's acquisition is a good fit with the Boating Camping Fishing brand and the larger Super Cheap Auto business continues to perform well. Super Cheap currently trades around $5.50.

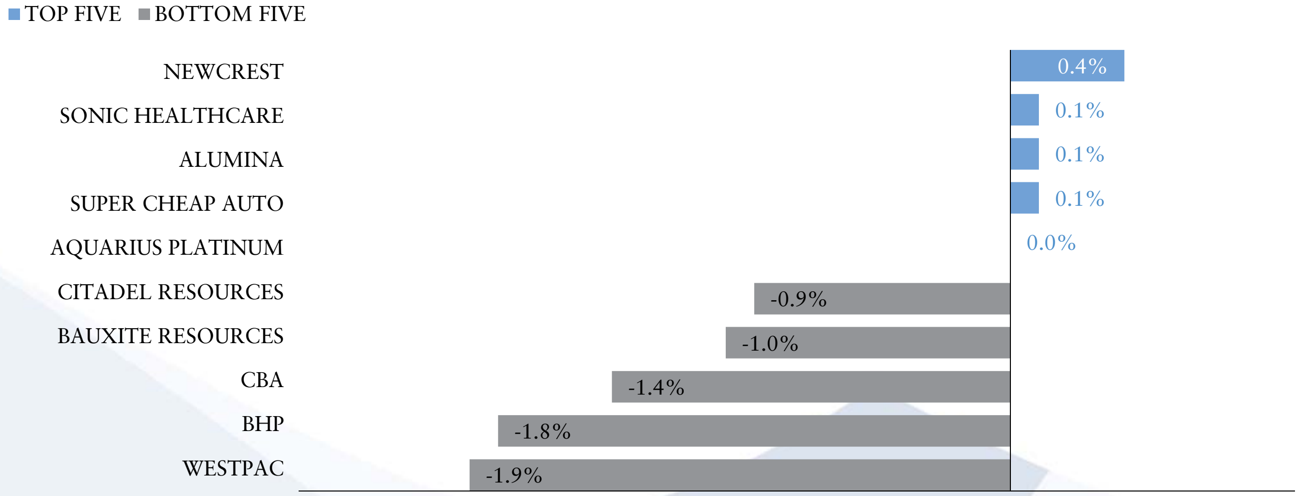
A position in Toll Holdings was established last quarter. Toll rates well in our qualitative Q stocks ranking and further purchases were made in May and June at prices well below our target valuation. We met with CEO Paul Little in June and expect Toll to benefit as the Australian economy continues to grow.

We also increased our AXA holding given it continues to trade at a significant discount to both previous bids from NAB and AMP. We expect that AXA will eventually fall to an acquirer given it is the last strategically important wealth management business of scale in Australia and the AXA Board has shown a willingness to sell. However, this takeover will take some time to resolve.

As before, the portfolio remains biased towards the largest stocks in the market with only 9% currently held in small caps. The structure of our portfolio means it does better in an environment of a weakening Australian Dollar.

Cash approximated 3% of the portfolio at the end of the quarter.

MAJOR CONTRIBUTIONS TO PORTFOLIO RETURN JUNE QUARTER 2010



OUTLOOK

THE RECENT MARKET SELLOFF HAS MEANT THAT VALUE IS STARTING TO EMERGE. THE MARKET CAN BE EXPECTED TO REMAIN VOLATILE AND TO TRADE WITHIN A NARROW BAND. CAREFUL STOCK SELECTION AND DISCIPLINE ON THE SELL DECISION WILL BE REQUIRED TO PROFIT IN THIS ENVIRONMENT.

At the time of writing, markets are staging a comeback, posting some large daily gains. This is perhaps a reflection that some companies now appear to represent good value, particularly when compared to history.

There are significant negatives to consider. These mostly relate to the flow-on effects of dealing with excessive debt levels and the imbalances these have produced in some economies. These are well documented concerns which have pre-occupied the market for the last few years.

A near-term hurdle is the upcoming release of results from the "stress tests" of European banks. These results may send a shudder of doubt through world markets if the European banking system is assessed as fragile and in need of recapitalisation.

In the US, recent rather anaemic economic data has raised questions about the sustainability of the recovery in the world's largest economy and what that means for global growth; the most pessimistic view being that the US slips backwards into recession.

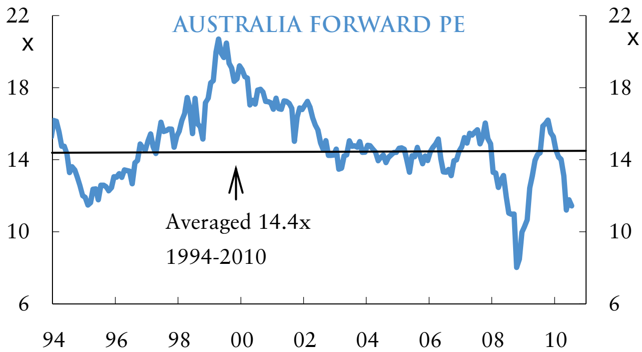
Most importantly, the spectre of a potential day of reckoning in the US due to its precarious level of government debt remains. The preferred path is for the US to grow its way out of debt, keeping both interest rates and inflation under control while it does so. It's a case of "so far so good" at present.

Markets, however, thrive on hope and it is quite possible we see strong positive moves on the back of any government action aimed at addressing or offsetting these financial imbalances.

It may be that the US government extends the current policy of near zero interest rates and perhaps announce a further round of fiscal stimulus. European bank stress tests may show that the financial system is adequately capitalised and the risks are manageable.

These sorts of developments can really move markets and are likely to be very positive for equities, at least in the short term. We are very attuned to such developments and the potential to profit from periods of weakness as well as strength.

We note that the more bullish analysts are saying that the Australian market is cheap at current levels (4,200 -4,400 points for the S&P/ASX 200 Index) even if you assume a significant downgrade to earnings in both 2011 and 2012. With the market trading at a P/E ratio of around 11x compared to the average of 14-15x of the last 15 years, some have targets of well above 5,000 for the ASX 200.



Source: Deutsche Bank; ASX200 ex resources and LPTs

Many stocks do appear to represent value with some trading at very attractive yields. Two of our largest holdings, Westpac (7.0%) and QBE (7.5%) are at record yields compared to recent years. A large number of our other investments are also trading substantially below our valuations, notably Oil Search, News Corp, Citadel, Transurban and Simsmetal.

Cyclical industrial stocks once again look cheap. In the early stages of the recovery last year, these stocks delivered impressive returns. In recent months, they have sagged and now trade at levels that suggest large earnings downgrades are just around the corner.

It is clear that much of the recent bounce back has lacked conviction with many share price moves occurring on very thin trading volumes. This highlights lingering doubts about the fragility of world markets. Many investors remain on the sidelines preferring to review the reporting season for a cue on the direction of future earnings.

Over a longer term horizon, we expect growth will be hard to come by and that dividends will contribute a greater proportion of an investor's total investment return. Shareholders in companies that demonstrate an ability to consistently grow earnings will be well rewarded. Finding these companies and buying at times of market weakness is the opportunity.

We rely heavily on our process and continue to act based on our target valuations. This is likely to mean that stocks are bought when pessimism is high and they are trading below our valuation, despite the prevailing market gloom. Just as importantly is that stocks are sold and profits taken when the market runs and target prices are reached.

In this environment turnover may increase and there might be periods where cash levels rise substantially.

As previously mentioned, more investment opportunities are opening up in domestically focused Australian companies. The Australian economy continues to perform with record low unemployment and little immediate threat to the continuing strong terms of trade it enjoys courtesy of our buoyant exports.

There is a large and impressive list of pending capital projects in mining, oil and gas and infrastructure. China remains an important driver of this investment and despite the likelihood of short-term hiccups in the Chinese growth path, benefits should continue to flow to Australian resource companies and those that service them.

With the resource super tax now modified, the risk of significant delay or cancellation of some of these projects has lessened. Even if some of the large capital works don't proceed the total spend is likely to be large and will add further to domestic activity, benefiting a number of industries.

Banks also look interesting given current market prices. However, banks are now probably best viewed as yield based trading stocks to be sold whenever target prices are met. They enjoyed a large earnings boost as charges associated with impaired assets fell as the GFC receded. With this now behind them, earnings growth is likely to remain stodgy. There are also limits on the availability of offshore funding. In this environment, credit growth should be diminished thereby capping the price we are prepared to pay for banks generally.

We are conscious of the threat of higher interest rates and the potential for higher labour costs to impact earnings and valuations. The Australian dollar is closely tied to the path of global GDP and is something we watch very closely. We factor in each of these elements when assessing target companies.

Overall, it is a difficult environment and it is tough to consistently get it right quarter after quarter. We expect ongoing volatility and the market to continue to trade within a narrow band whilst the threats to the world's economies are worked through. Discipline in buying and selling will be important in the coming months.

FEES

No performance fee was earned during the quarter. Clients should note that a high water mark has been established with respect to any performance fee. This means that no performance fee will be earned until the portfolio value exceeds the high water mark and the performance hurdle is met.

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