QUEST

QUARTERLY REPORT
MARCH 2009

John Citizen

QUARTERLY REPORT
MARCH 2009

Mr John Citizen	123 ABC Street Sydney NSW 2000
Account Name: John Citizen	

PORTFOLIO MOVEMENT –MARCH QUARTER 2009	
PREVIOUS MARKET VALUE 31 DECEMBER 2008	
CONTRIBUTIONS DURING QUARTER	
PORTFOLIO MOVEMENT*	
MARKET VALUE 31 MARCH 2009	

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

*Includes fees for the quarter

MARKET SUMMARY

The market return for the March quarter was 1.9%. The Quest portfolio delivered a slightly better result and the portfolio remains close to the same value as at the start of the quarter.

January and February were difficult months and new market lows were established in early March. The market stabilised late in the quarter as the degree of deterioration in economic data slowed.

At the lows, sentiment was dreadful with concern focused on the rapid decline in GDP in all of the world's major economies, rising unemployment in the US and the risk of sovereign collapse in Europe.

Governments stepped up the scale of support for their deteriorating economies, enacting enormous fiscal stimulus packages to arrest the slide in consumer and investor sentiment.

As central banks had already dropped cash rates to historic lows, the UK and US governments turned to printing money, using so called "quantitative easing", to address the ongoing weakness in credit markets and to help lower mortgage rates. These were extraordinary announcements and the market responded positively. There a myriad of unprecedented actions now being undertaken worldwide and are evidence that Central Banks and Governments will do whatever it takes to get economies moving again.

Companies rushed to raise new equity during the quarter to recapitalise balance sheets and allay the concerns of their bankers.

Property Trusts were particularly active. Most issues were made at a significant discount to the prevailing share price and many early issues traded straight down to or below the new issue price.

Equity issues later in the quarter performed well, giving confidence to the market and to other companies considering raising equity.

As expected, the February reporting season delivered deteriorating earnings and resulted in analysts revising their estimates for the full financial year down further. It has taken some time for analysts to reflect the full extent of the economic downturn in their forecasts. With FY09 earnings estimates now some 15% below FY08, expectations are now much more realistic. Fiscal year 2010 forecasts still appear to be too high. We expect these estimates to be reduced further with the impetus likely to be the run up to the August reporting season.

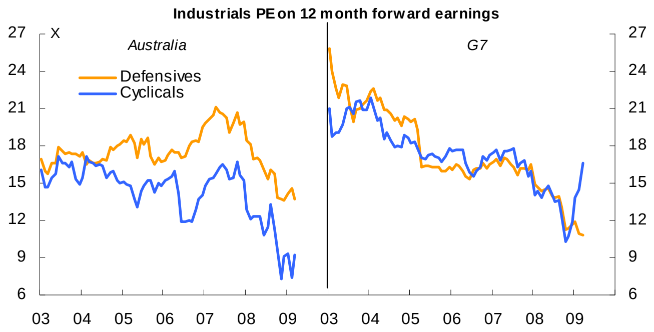
Recent economic data remains poor however the flow rate of negative economic data has slowed while the level of negativity built in to share prices is very high. Credit markets have shown signs of improvement with good levels of corporate bond issuance and some early easing in credits spreads. This is crucial to the re-establishment of corporate activity.

As a result, the end of the quarter saw the market swing to a more positive stance with March returning a very welcome positive 8.1% return. The March rally had considerable strength and continued into early April. At the time of writing, the Australian market is 20% up from its low in early March while the US is up 24%, Japan 25% and China 33%.

Positive returns first occurred in the Chinese market and in commodities, both of which bottomed late last year. As confidence returned, the market sought out cyclical exposure amongst stocks that had collapsed, particularly the juniors.

Quest previously benefited from large holdings in well run defensive companies that are less sensitive to the impact of an economic downturn. During the quarter we added more cyclical exposure to the portfolio as we recognised that these stocks had been sold down to fire sale levels.

As the chart shows, the gap between the relative price of defensives versus cyclicals became extreme during January and February. The effect was more pronounced in Australia than in the rest of the world. Small stocks were also shunned in preference for the large, liquid majors.



Source: Deutsche Bank

Thus, when the market turned, the biggest gains were first seen in the cyclical stocks. The gains were rapid and in some cases very large with a number of small stocks doubling or trebling from their lows.

Resources, Energy and Financials fared the best during the quarter. BHP, RIO, Santos, CBA, WBC and Wesfarmers all posted strong positive returns. By contrast, the Property sector was off some 25%, reflecting the both the parlous state of the typical balance sheet and the level of uncertainty as to the true value of underlying property holdings.

PORTFOLIO ACTIVITY

Given the Government's efforts to stimulate the Australian economy, particularly housing, we have been attracted to low-priced, well-capitalised, domestically focussed companies exposed to either the consumer spend or to first home owner housing.

We bought Wesfarmers, JB Hi-Fi, IAG and Suncorp and sold all four within the quarter, profitably. We also built positions in Stockland and AMP.

Our positions in CBA, WBC, Santos and BHP benefited from the cyclical rotation late in the period, offsetting significant falls in QBE and Sonic Healthcare which fell due to their defensive nature.

We also sold a number of stocks into market strength as our price targets were met or where we had concerns about the sustainability of the price moves. We exited ANZ, NewsCorp, Felix Resources and Worley during the quarter.

New portfolio positions were established in AXA (via a placement in March) and OneSteel and we added to our investments in ASX, CSL and Charter Hall. Charter Hall has more than doubled since our purchase at its all time low.

The extreme volatility and bearishness early in the quarter allowed us to add to our position in WDS Limited. WDS is a small cap pipeline/mining services company serving the participants in the coal seam methane development in Queensland. Shares were purchased below $0.50 and subsequently traded up over $1.00.

We recently visited 23 companies in Perth over 3 days and added Mermaid Marine to the portfolio as a result. Our meetings and research led us to the conclusion that the Gorgon gas field development on the North West Shelf (Chevron, Exxon and Shell) is likely to proceed with project expenditure expected to total A$50bn. This will be Australia's largest ever project, even larger than the recently announced Rudd NBN rollout! Mermaid Marine controls strategically important port and shipping assets that will be critical in any development of this gas field. The stock has already contributed to the portfolio with a handy gain since purchase.

OUTLOOK

After pondering market risk for an extended period, investors have started to think again about the potential for upside. Market views are heavily polarised, from ‘sell the bear market rally’ to ‘the next bull market low has been seen’.

Whilst Quest is not expecting the near-term economic news to get significantly better, we believe that the market is unlikely to breach the lows established in early March. In addition to the magnitude of the fall in share prices, there is now massive global fiscal and monetary stimulus in the system. Credit markets are slowly becoming more liquid, Australian banks are financially sound and the real income of the average Australian household grew 10% in the December quarter. All of this suggests that an investment in the market at this time will be rewarded over the medium-term. We believe the majority of our major investments will not breach recent lows.

The most attractive opportunities now appear to be in small caps and we envisage further increasing our exposure to smaller companies. Our current small cap industrial holdings include Seek, Australian Wealth Management, WDS Limited and Mermaid Marine.

Banks still face some challenges ahead as impairments continue to rise. We think the process of recognising and digesting bad loans will take longer to run and cause more uncertainty than is currently expected by the market. Our preferred banks remain CBA and WBC based on the quality of their loan book and the likelihood that the strongest banks will benefit most once the economy regains its footing.

A large number of Property Trusts are expected to breach their debt covenants in the near future and this is reflected in beaten down share prices. We continue to closely review investment opportunities in this sector. Our property holdings are Stockland and Charter Hall.

Clients will be aware of our continued lack of interest in Telstra. We have been concerned about falling returns, poor customer service and valuation. The recent government NBN announcement now adds a new competitor with a seemingly unlimited investment capacity and a focus on delivering a product for the voter. The lack of focus on return from the NBN only increases our concerns regarding Telstra.

We are not convinced that the recent rally in the resource sector will continue. Global Industrial Production continues to weaken whilst stockpiles grow. Freight cost indicators have again turned down.

We have been trimming our exposure to the Energy sector taking advantage of recent higher prices.

Gold is also of concern as it appears the “flight from risk” has caused a bubble to develop. Physical gold holdings by global gold funds are at all time highs. We do not believe these funds are natural owners of this commodity and gold stocks appear to be at unsustainably high values.

Overall, the Quest portfolio has performed significantly better than the market during this downturn and we aim to continue this as the market recovers. We are now of the view that the current market presents an opportunity for investors with an investment horizon of two years or more. We welcome enquiries from any clients considering an additional investment with Quest.

FEES

No performance fee was earned during the March quarter.

Clients should note that a high water mark has been established with respect to any potential 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.

CONTACT QUEST

Quest Asset Partners Pty Limited

ACN 109 448 802

AFS Licence No. 279207

Suite 706, 6A Glen Street
Milsons Point NSW 2061

Telephone:	(02) 9409 2333
Email:	askus@questap.com.au
Web:	www.questap.com.au

IMPORTANT NOTICE

These comments are of a general nature only. In preparing this report Quest has not taken into account an individual's investment objectives, financial situation and particular needs ("financial circumstances"). Accordingly, this report should not be relied on.

Past performance may not be a reliable indicator of future performance.

Quest holds an AFS wholesale licence number 279207. Quest is not available or appropriate for retail investors. This information is not to be passed on to retail investors.

Neither Quest Asset Partners Pty Limited nor Goldman Sachs JBWere Capital Markets Limited guarantees the performance of the fund, the repayment of capital or any particular rate of return.