

**Live well. Sleep well.**  
2011 Annual Report to our clients



2011 Annual Report



## FOUNDER'S LETTER

***“The provision of individual, indispensable and enduring relationships that create, manage and protect wealth”***



Dear client

### Another successful year

For the second successive year since the GFC our clients enjoyed good positive returns.

The chilly Siberian winds that hit the markets late in the year could not overwhelm the strong returns from the earlier part of the year.

Up until April, the share market had gained strongly on the back of the sound outlook for Australian shares.

But then short-term perceptions about the global economy (is the US going into recession? will China slow-down? etc) or localised events (will Greece default?) unnerved investors.

Well, unnerved short-term investors.

Long-term investors see past short-term perceptions, and look for sustainable and fundamental value.

We are long-term investors, because our clients invest for the long-term.

As Warren Buffett said,

***“The stock market is designed to transfer wealth from the active to the patient.”***

And so 12 months ago, when the share market also had conniptions (curiously over the same unresolved issues that seem to spook some investors today), we chose to ignore the emotion and remain virtually fully invested.

This was because our investments met the three fundamental tests we have (see opposite).

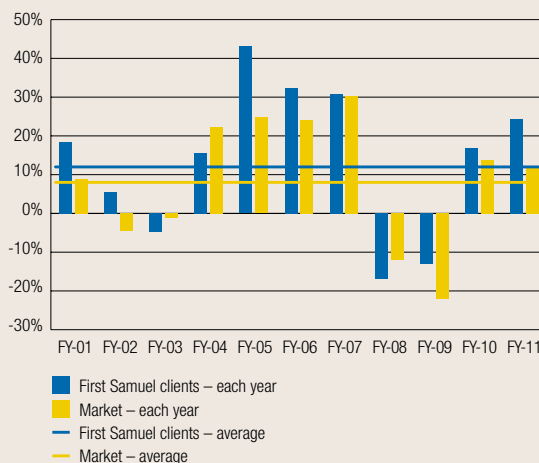
And as you can see from the charts, our clients were well rewarded.

### Outlook: Greeks throwing plates doesn't matter

I'm not sure whether it's curiosity, boredom or just a need for instant information, but the increasing focus on *news* rather than *information* is vexing.

News reports are designed to appeal to our emotions – be they joy, despair, remorse, elation or whatever.

**Share markets are always volatile – the last decade is no exception. Better to look to the long term. And sleep well.**



Markets is All Ordinaries Accumulation Index (i.e. share market including dividends). First Samuel clients is the weighted average of all clients' share performance before fees. Past performance is not a guarantee of similar performance.

And so during the past fiscal year we have seen news triggering emotions. And the emotional response to the news itself triggers share market activity. Or share market concerns.

The curious thing is that when the market/ short-term investors get in a mind set, it is hard to change it.

So the past year has been a bad news year. And almost every piece of economic/ market/ investment bad news, no matter how relevant (i.e. information), has been greeted with a negative response. And good information has been overlooked.

In the years leading up to the GFC, it was the reverse. Everyone was looking for good news, and bad information was dismissed.

We take the view that it is the *information* that matters, not news.

And so we are not concerned about the Greeks and their parlous fiscal situation (except from a pastoral point of view).

We are only concerned with the things that matter.

And there are just three<sup>1</sup>.

### Outlook: only three things matter

A focus on *sustainable income* from investments, as we note more fully in our Investment Review (from page 22), be it from shares or income securities, is the first part of success.

Secondly, with shares, investors also get the benefit of the *growth in those dividends*. It is the growth in dividends that drives higher long-term share prices. And hence the long-term capital gain that share investors seek.

And third is *buying those investments when they are cheap*.

On those three bases we are quite comfortable with the outlook.

So, we, and you, can ignore the seeming volatile macro-economic uncertainty. And sleep well.

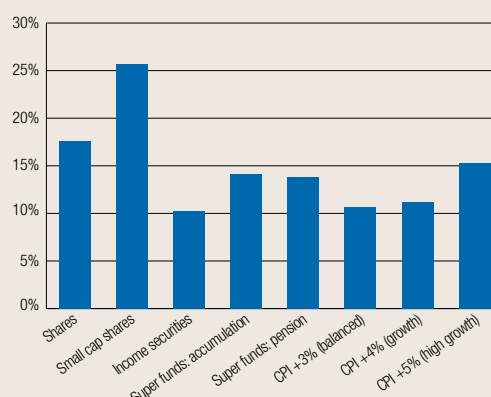
### Good year for all clients

In spite of all the seeming poor news, First Samuel clients had a very good year.

All client portfolios are individually managed, so each client's overall return after-tax is going to depend upon each portfolio's:

- mix of asset classes
- asset class performance
- the tax rate applicable to the portfolio
- management of tax.

A good year. All First Samuel portfolio types returned well in excess of benchmarks, after fees\*



\* Average of all like portfolios, after fees, before tax. All portfolios are individually managed so individual portfolio performance may differ. Past performance is not a guarantee of similar performance.

But it is clear that the excellent performance of the underlying asset sectors means that total performance of each client's overall portfolio exceeded expectations after fees (see chart).

And for all portfolios, our tax management has added measurably to after-tax returns (even for non-taxpayers, where astute use of share buybacks and franking credits has added after-tax value).

Of the major asset classes, First Samuel **Australian shares** returned an average of over 17% for the year, after fees, somewhat well ahead of the market's 12%<sup>2</sup>.

In eight of the past 11 years our Australian share performance has been positive (and two of the negative years were during the GFC), something that cannot be said for the sharemarket overall.

**Australian shares' small caps** had another exceptional year, returning an average of 26%, well ahead of the 16% return of the Small Ords Index.

And clients with income securities also had a strong year, returning on average 10%, well ahead of the average bank bill rate of 5%.

Please see your individual Investment Report from page 22 for more information.

<sup>1</sup> Of course, the reality is that it is not that simple – investment management is complex. Which is why self-management is not viable.

<sup>2</sup> Both figures include dividends.

## FOUNDER'S LETTER

### At First Samuel

#### Associates...

As you can see from the photo on page 1, First Samuel is more than three or four people.

Our team of 16 Associates serves you with skill, responsiveness and respect. I am grateful for their service to you and their enthusiasm and focus.

It is a delight to me that at all times our team has shown respect for you and for one another, always acting in a highly professional manner.

#### **Strategy: tailored and dynamic advice and structuring**

Nikki Hill  
Duro Rudic  
Simon Devlin  
Jack Ngo  
Jenny Forbes

#### **Investment: individual and long-term after-tax**

Dennison Hambling  
Fleur Graves  
Craig Fraser  
Emma Coote  
Cameron Blackwell

#### **Administration: timely, accurate and useful**

Joe Flinn  
Susanne Retallick  
Zoë Borg  
Kelly White

#### **...and client advisers**

Roy Leech  
Anthony Starkins

***"I enjoy working for First Samuel clients because they are looking for the type of prompt, personal and professional customer service that I take pride in providing."***

*Susanne Retallick, Business Manager, First Samuel*

#### Management...

So too, our Leadership Team.

Joe Flinn runs First Samuel with all the efficiency and attention to detail of a Scottish accountant.

And my thanks to him and also to Dennison Hambling, our CIO, and Nikki Hill, Head of Strategy, for their strategic thinking, responsiveness and concern for our clients.



#### ... and Board

I have said many times that we have, arguably, the finest board of directors in Australia for a company of our size. And I thank Murray Baird, John Bryson, Tony Greenwood and Elizabeth Parkin for another most successful year. Their guidance, thoughtfulness and client focus is a boon for us.

And there has been one change. Our Chairman for the past 10 years, Nicholas Barnett, has decided to retire. I am most grateful for his guidance, wisdom, encouragement and leadership of First Samuel over our first decade.

He will be missed.

I am delighted that Murray Baird agreed to succeed Nick. Murray is an experienced director, with a considerable background in the law and not-for-profit organisations.

#### Shareholding

Part of the culture of First Samuel is to ensure that there is an alignment of the long-term interests of our clients, our Associates and my family company.

And so you should be aware that about 20% of the equity in First Samuel is owned by our senior Associates.

#### Client service

Our relentless focus on client service has been rewarded by us receiving very high ratings in our annual client survey. And most demonstrably by our high client retention rate and willingness of our clients to refer their family, friends and colleagues to us.

There can be no finer measure of service.

All my colleagues and I look forward to serving your needs for many more years.

With kind regards



**Anthony Starkins**  
Founder and Executive Director

## A unique service – an ethical business

We have a fiduciary relationship with you and each of our clients. It is both our responsibility, and desire, to serve your interests, not our own.

In practice this means:

### This business will not quickly grow

We do not seek to be the largest or most profitable in anything. Too many businesses are born, flourish and then die because they sought to grow quickly. They forgot about their clients.

Because of our family shareholding, we can focus on longer term sustainability for our clients.

We are not distracted by short-term profit goals, or the need to justify ourselves to the broader media, the public or widely dispersed shareholders.

### Commissions are unethical

Our view contrasts starkly with the traditional practice of advisers steering clients towards

managed funds, wrap accounts or master funds because of the upfront and trailing commissions they receive for so doing, or towards non-discretionary brokers who might pay a rebate.

The investments we make for you are selected because they will meet your needs, not because they will earn us commissions.

Any commissions we unavoidably receive from third parties for managing your investments will be passed onto you, in full.

### Full disclosure and transparency

We have a policy of full fee and cost disclosure. These are set out clearly in our Financial Services Guide. There are no hidden charges or fees.

We tell you the way it is – not all investment decisions will be successful and we will tell you when we have made decisions that have not met our expectations.

## A unique service – a focused, intentional company

### Wealth management doesn't just happen

Creating the wealth to live well now and in later life doesn't just happen. It results from thoughtful and skilled advice, diligent planning, wise investment, regular attention and good administration.

Your wealth exists in a world that's fast-changing, complex and highly regulated.

In this environment, wise investors understand that an integrated, comprehensive and professional service almost certainly provides the best avenue for creating, managing and protecting their wealth.

### Traditional European private bank

First Samuel is a boutique specialist investment house. We have fashioned ourselves along the lines of the traditional European private bank and have mastered the art of successfully integrating the four critical areas of wealth management:

- strategic wealth management planning and advice
- tailored and individual investment management
- administration, reporting and auditing, and
- an embracing ethical overlay.

### Our only business

Individual wealth management is First Samuel's only business.

We are not part of a larger financial service such as banking or broking.

We are not a financial planning company that uses tied administration "platforms" and invests in managed funds.

Our focus is purely on the provision of individual, indispensable and enduring relationships that create, manage and protect wealth.

*"First Samuel allows me to provide the highest quality advice and service to clients without restriction or the need to sell particular products."*

*Nikki Hill, Head of Client Strategy, First Samuel*

## OUR BUSINESS

# A unique service – 10 dimensions of wealth management

### We see wealth management differently.

It is answering “yes” to these 10 basic questions. Each question is a dimension of wealth management. And together the 10 are the framework upon which we have placed our total relationship with you.

#### 1. Have you a dynamic, long-term strategy?

You need to know where you are today and to where you wish to go. Even at its most basic, wealth management must have strategy or a plan.

#### 2. Have you invested, not saved?

The simplest dimension is to use your savings to invest. Investing is putting to work for the long-term that which you have saved or can save.

#### 3. Have you protected yourself/ managed risk?

Assets (including your life) are vulnerable to unforeseen events that diminish the value of that asset and the income it produces.

Assets need to be protected, either by diversification or other techniques (for investments) or insurance (lives).

#### 4. Have you deployed superannuation, and other structures?

You now have access to an almost uniquely Australian wealth management tool: self managed superannuation. This has added an extraordinary dimension to wealth management.

And of course there are other structures: trusts, companies, etc that can also be used.

#### 5. Have you optimised tax?

Your biggest expense in life is tax. Far bigger than investment fees, school fees or accountant's fees.

Optimal tax payment comes from sensible structuring, use of individual portfolios and active management.

#### 6. Has information been wisely used?

Because we are all so much more aware of economic and markets events – to the point of virtual instantaneousness – we react differently than if we had more time to reflect upon new information.

Hence, whilst there has always been the madness of crowds (Dutch tulip bulb craze, South Sea Bubble, etc), now there is more, the contagion of hour-by-hour information.

Far better to use information wisely. On your terms. And to your needs.

*“I make a difference for our philanthropic clients by understanding that what is important to them is just as important to us.”*

*Roy Leech, Private Client Adviser, First Samuel*

#### 7. Have you been wary of government?

Sadly, and most pervasively, the role of government is having an increasing effect on the ability to manage wealth.

This includes tax, regulatory changes, economic policy, pensions and corporations' law.

#### 8. Can you measure and compare?

You should not be content with just knowing the value of your wealth.

You want to know how your wealth is changing. After fees. After tax. And compared to your benchmarks. And all of the details.

#### 9. Have you respected your legacy?

You will not know when you are going to “shuffle off this mortal coil”.

So you need to plan, now, how you wish your net assets disposed of when you do. Or before you do.

#### 10. Have you been treated ethically?

None of the preceding nine questions is worthy of a Yes, if the last one is answered No.

We will take care of all of the above for you, by answering the “how?”



## A unique service – two examples of the 10 dimensions of wealth management

We set out on the following pages two examples of where we blend several of the 10 dimensions to meet client needs.

In so doing we use each of our three core services:

- Strategy advice
- Individual investing
- Comprehensive administration

And because these services are fully integrated within the one company, we can ensure the most efficacious outcome for our clients.

### Self Managed Superannuation

Superannuation remains the most tax effective investment vehicle for many people.

But many of the tax advantages of super can be seriously eroded if you invest in an industry fund, corporate fund or public offer fund.

For maximum long-term outcomes, a self managed superannuation fund may be the best option.

### Retirement Strategy and Investing

We call it “getting to the other side.”

Too often people leave their retirement strategy until it is too late.

Too late to put the most optimal strategy in place.

Too late to ensure that there is enough capital upon which to live without the back up of a salary or wage income.

Too late to consider complementing super investments with those outside of super.

### Other strategy dimensions

But there is more to strategy than superannuation and retirement planning.

Some other strategy services we provided include:

- Salary packaging and structuring
- After-tax capital adequacy mapping
- Cash flow mapping
- Debt restructuring
- Life, income protection, etc (insurances)
- Entity structuring
- Recommending the right asset allocation
- Regulatory monitoring
- Leverage strategies
- Estate planning

The point is that each service falls into one or more of the 10 wealth management dimensions. And for each client, our service offering of the 10 dimensions is indispensable.

You can be an indistinguishable superfund member – crushed, panicked, driven by the herd.  
Or you can be free. And control your super.

First Samuel Self Managed Super.  
Capture the opportunity.

First Samuel

Around age 50 you will be confronted by a maze.  
The maze of moving from work based income to investment-based income.  
You need to know the maze exists.  
You need to make the right choices.  
So you can get to the other side. Easily.

First Samuel Retirement Strategy & Investing.  
Getting you to the other side. Easily.

First Samuel

## STRATEGY

# First Samuel Self Managed Super. Capture the opportunity.

### Super funds care about you and your family. Really?

In an industry super fund (e.g. Health Super) or public offer fund (e.g. BT Super) you are one of many hundreds of thousands of members.

Your investments are in commodity funds managed by agglomerative managers whose main concern is not you and your family's long-term after tax wealth.

You are distant from your investments. And have little control.

Hmm. Is there a better way to capture the super opportunity?

### You do have a choice

Choosing the wrong type of super could cost you hundreds of thousands of dollars by retirement age.

You choose the car you drive.

You choose the house in which you live.

Shouldn't you choose your super?

*"I enjoy working for First Samuel clients because I care about their wealth management success."*

*Cameron Blackwell, Portfolio Administrator, First Samuel*

### Exercise that choice

The government allows individuals to have their own super fund, called a self managed superannuation fund (SMSF). You may have heard about these. Or even have one yourself.

This means that you can control your super.

It's your super fund.

### See the difference

There are many differences between the various super fund alternatives. The chart below highlights some of the differences.

The choice of which one best suits your needs is easy.

Of course, before acting on your choice you should take personal advice from a qualified adviser.

#### Super fund types – what suits your needs?

Your needs	First Samuel Self Managed Super	Basic SMSF	Industry super fund or Public offer super fund
Control over your super	Yes	Yes	Limited
Tax efficiency	Highest possible	Possible	No
Investment choice	Maximum flexibility	Maximum flexibility	Limited
Investment by an expert	Yes	Maybe	Maybe
Full integration of super investment with advice and administration	Yes	Possible	No
Full integration with non-super advice, investment and administration	Yes	Possible	No
Super contributions monitored to ensure no limit breaches	Yes	Possible	No
No CGT on move to pension phase	Yes	Yes	No
Ability to borrow in super	Yes	Yes	No
Ability to invest in direct property	Yes	Yes	No
Total transparency of fees and costs	Yes	Yes	No
Total transparency of each transaction	Yes	Yes	No

## Do you have the time, ability or commitment?

If having a SMSF is the best super alternative for you, you should reflect on whether you have the time, ability or commitment to undertake all that needs to happen in a SMSF.

In reality, you probably don't and haven't.

There is little point in putting at risk the significant tax concessions that a SMSF has because of an administrative error.

Equally, compromising optimal after-tax long term investment performance because you think you are an astute investor is not so smart either.

And taking strategy advice by reading a financial planning magazine or financial pages of a newspaper or by listening to a mate over a dinner table seems somewhat, well, daft.

Better to enhance the opportunity of your SMSF by appointing an expert.

## Mistakes we have seen

Nobody is perfect. But people come to us whose management of their SMSF has cost them dearly. Some of the more common mistakes are:

### Not tracking contributions

Not keeping track of super contributions and thus exceeding the limit. Thus paying more tax.

### Excited about art

Investing in an art leasing deal, with the hope of both regular income and capital gain. But no-one would rent the art.

### Lazy super

Keeping over 50% of the portfolio in cash. Thus missing the benefits of investment growth and condemning the portfolio to lose value after inflation.

### Greedy super

Investing most of the portfolio in tax-driven and leveraged investment schemes. But the portfolio lost 85% of its value.

### "Gotta great tip!"

Buying a share on a "tip", but no-one told him when to sell. Thus lost 60% of the shares' value.

### More funds than sense

Investing in more than 15 managed funds. Thus diversifying away any possible value added. As well as paying large fees.

And so it goes on.

### First Samuel Self Managed Super – just some of the things we do for you

Advice on SMSFs – including all regulatory matters	✓*
Your SMSF establishment – all documentation preparation and submission	✓*
Arrange accountant (if you don't have one)	✓*
Advice on your super strategy – contributions, packaging, etc	✓
Advice on your SMSF – including estate planning, investment strategy, etc	✓
Advice on choosing First Samuel Self Managed Super	✓
Handling of all rollovers and transfers, ensuring accurate documentation	✓
Ongoing advice both for your SMSF and also for other wealth management needs	✓
Individual tailored and direct investment management (ask for more on this)	✓
Pension payments (if in pension phase), tax and accountant payments	✓
Comprehensive administration, statutory reporting, etc	✓
Regular investment commentary, etc	✓
Secure internet access to daily updated reports on all your portfolios	✓
Independent audit certificate	✓

\* If you don't have a SMSF

### First Samuel Self Managed Super. Capture the super opportunity.

Many people fail to use their SMSF to its maximum opportunity for so many reasons.

But there is a way to capture that opportunity.

First Samuel has been managing SMSFs for over a decade.

We have earned the trust of our clients to manage all aspects of SMSFs.

Talk to us. Or visit [www.firstsamuel.com.au](http://www.firstsamuel.com.au)

**STRATEGY**

# First Samuel Retirement Strategy & Investing. Getting you to the other side. Easily.

*So, you are about 50 and thinking that you have another 15 years before retirement?*

*And so 15 years before you need to think about it.*

*Right?*

**Wrong.**

The complexity of the Australian superannuation system means that from around age 50 you need to start considering the choices in front of you.

Yes, I know you plan to work until 65 or 70.

But there is lots of upside from doing a little planning.

Delay will be costly.

## Why start planning around age 50?

### 1. Plan for age-based rules and tax variations

Because the first of the government age-based rules comes into play at age 50, you need to plan in advance for that opportunity.

### 2. Plan to move from work-based to investment-based income

From about age 50 to about age 60 is the peak income earning years for many people.

So you need to plan how you are going to balance this income between your short-term and long-term needs.

*Retirement strategy is not about silver haired couples walking along the beach, hand in hand. That is for people in retirement.*

*Retirement strategy is the hard reality of how to move from work-based income to investment-based income.*

*How to get you to the other side.*

*Given the complexity of super in Australia, that means making decisions around age 50.*

*Delay will be costly.*

That is to say, you need to consider how you are going to move away from living off work-based income to living off investments.

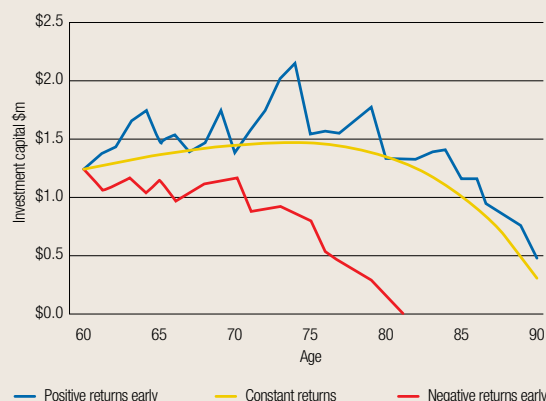
If you leave the planning too late, you may find yourself with too little investments from which to live for the next 30 or 40 years.

## Getting you to the other side. What age-based rules apply, and when.

Age	50	55	60	65	75
	<ul style="list-style-type: none"> <li>Transitional annual concessional super contribution limit of \$50,000 until 30 June 2012 (thereafter \$25,000 indexed).</li> </ul>	<ul style="list-style-type: none"> <li>Preservation age* and permanently retired: full access to super benefits. Taxable components of benefits taxable.</li> </ul>	<ul style="list-style-type: none"> <li>All super lump sum withdrawals or pension payments are received tax-free.</li> </ul>	<ul style="list-style-type: none"> <li>Fully access super benefits (even if continuing to work).</li> <li>Need to meet a work test to make super contributions.</li> </ul>	<ul style="list-style-type: none"> <li>No longer make super contributions (excluding mandated employer contributions).</li> </ul>
	<ul style="list-style-type: none"> <li>Annual concessional super contribution limit of \$50,000 if total superannuation balances below \$500,000 (proposal from 1 July 2012).</li> </ul>	<ul style="list-style-type: none"> <li>Preservation age* and still working: can commence a 'transition to retirement' pension.</li> </ul>	<ul style="list-style-type: none"> <li>And terminating an employment agreement: fully access super benefits.</li> </ul>	<ul style="list-style-type: none"> <li>No longer able to use 3-years-in-one rules for non-concessional contributions.</li> </ul>	

\* (age 55 until 2015 then increases from age 55 by a year annually until 2024)

Even super of \$1.25m projected to last well past age 90 may be exhausted soon after age 80 (see text)



*The maze is before you.*

*On this side of the maze is your work-based income.*

*On the other side is investment-based income.*

*You need to get to the other side.*

The maze that confronts you has at least seven shifting elements:

#### 1. Government

The age-based super rules, SMSF rules, tax variations.

#### 2. Investment-based income

Your desired income from investments is an after-tax, inflation adjusted figure.

#### 3. Work-based income

Your current income from your day (or night) job will be the basis of your investment-based income.

#### 4. Work

For how long do you plan to work?

#### 5. Risk

See the chart\*: three retirement portfolios each have the same average long-term return. One has negative returns early on, another positive returns early on and the last has constant returns. Capital will be exhausted by age 81 in the first case. The correct asset mix is the answer.

***“You do not want to spend time worrying about your investments or the latest government super regulations.”***

\* Assumes capital of \$1.25m, 8.6% p.a. average return, \$75,000 pension indexed at CPI of 3.5% p.a., commencing at age 60.

#### 6. Non super

Your non-super structures and investments must be considered.

#### 7. Death consequences

Your estate planning desires are critical. For example, your super is not directly covered by your will.

### Be afraid. Be very afraid. Of:

#### A. Capital exhaustion

Running out of capital before you die is perhaps people’s greatest fear. For example:

- the wrong asset allocation may see the portfolio capital vulnerable to a sharp market fall (see chart)
- spending too much now of work-based income and not leaving enough to invest in investment-based income
- poor investing; either taking too much risk or not enough

#### B. Paying too much tax

Failure to understand the opportunities and traps of the complex interaction of superannuation tax, capital gains and personal tax can lead to you or your estate paying too much tax.

#### C. Undue complexity

The transition to investment-based income should be worry free and without hassles.

#### ***First Samuel Retirement Strategy & Investing. Getting you to the other side.***

Getting our clients to the other side is exactly what we do. And do well.

By offering an individual and integrated service of:

- Advice
- Investment
- Administration

Whether you choose to spend more worry-free time on the things you like to do, not on things you have to do...

Or you choose to keep working past age 55...

We will take all the worry from you.

First Samuel has been doing this for over a decade.

We have earned the trust of our clients to manage all aspects of transition from work-based income to investment-based income.

***Talk to us. Or visit  
www.firstsamuel.com.au***

## INVESTMENT

# A strong year – with more than a little déjà vu.

### The share market

In a year similar to last, strong returns were generated.

The first seven months of the year drove the market's strength.

The Australian economy was in robust health, with the benefits of the booming resources sector cascading throughout the economy.

However, massive floods in Queensland in January disrupted that state's economy to a considerable degree, especially its mining sector.

Then the Japanese tsunami and its nervous aftermath and concern about unrest in Libya / other Middle East / North African countries began to soften confidence.

And so the market struggled to a peak for the fiscal year on 11th April.

Since then, four things spooked the market. (We were, and are, not too concerned about these things).

Our focus has been more on longer-term and fundamental matters that affect your investments.

And the negative affect these four things have had on the market and on sentiment just made the market undervalued.

#### 1. Sovereign debt generally, Greece in particular

Greece is a small part of the world economy, being just 0.5% of global GDP.

However, there was concern at the outcome if Greece defaulted on its debt obligations.

The potential impact on the Euro currency union, as well as on European banks and their financial system, caused considerable uncertainty in the markets.

#### 2. US, needing more growth

Notwithstanding the upward but patchy rise in GDP and GDP outlook, the most telling indicator of health in the US economy, and the most politically important, is the rate of unemployment.

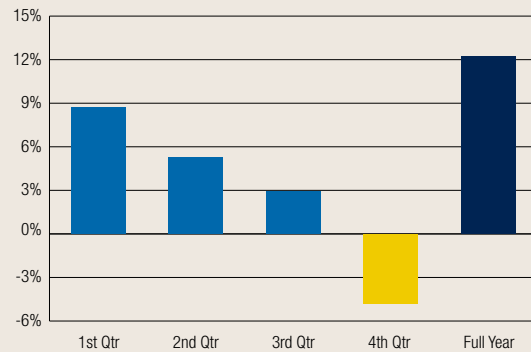
This rate has now gone back to over 9%.

This is certainly a bad sign for the President. But fewer people in work means less effective consumers. And as consumption is the largest part of the US economy, a high unemployment rate is going to put sand in the wheels of economic recovery.

#### 3. China, wanting less growth

In contrast to the US, China is attempting to engineer a slower rate of economic growth.

In spite of the soggy end to the year the market still returned over 12%



This is because of inflationary fears. In particular, the sharply rising price of food items is a major concern.

And so China tightened availability of credit and increased interest rates.

#### 4. Want of economic leadership in Australia

The decline in consumer confidence that fed into share market nervousness was driven as much by domestic political consideration as international macro-economic matters.

At the best of times, a minority government causes uncertainty. But this uncertainty was exacerbated by the upcoming carbon tax announcement.

With doubts as to the structure of the package and fierce opposition to it, short-term investors preferred to sit on their hands – accumulating cash or moving to other asset classes.

#### Market up 12.2%...

The final result was that, carried by success in the early part of the year, the Australian share market (including dividends) rose a strong 12.2%.

#### ...but undervalued

However, the 4th quarter share market weakness, for reasons other than the future profitability of Australian shares, meant that we exited FY-11 with a fundamentally undervalued stock market.

That is to say, the price of \$12.10 to buy one dollar of next year's profit was much lower than its long term average of \$14.70.<sup>3</sup>

So, notwithstanding the current uncertainty, we end the year in a better position than when we started:

- a strong year's return behind us, and
- a cheap market ahead of us.

<sup>3</sup> This is a layman's view of the jargon used in the industry to describe the Price/ Earnings ratio. The market would say that a company (or the market) is trading on 12.1 times earnings (i.e. profits). We are talking about the same things. The lower the P/E of a stock or a market, the cheaper it is.

## Your shares

We outperformed the market by a good margin over the full year.

The performance of the average Australian share portion of clients' portfolios was about 17%, after fees, some 5% ahead of the market.

Of course, individual performances vary with individual asset allocations – most clients have other asset sectors in addition to shares in their portfolio.

### As usual, there were good results...

Just thinking about our main criteria for stock selection:

1. predictable and strong dividends;
2. growing dividends (because of growing profits); and
3. cheap (generally as measured by P/E)

...it is clear to see areas where we don't have investments.

Because we are concerned about the growth of the dividends of banks we do not hold bank stocks – the banks had a modest year, returning on average about 2% less than the market.

We also do not hold Telstra, notwithstanding its high dividend yield, because we cannot see its dividend growing significantly. Telstra had a negative year.

Our concern about the expensive price (i.e. high P/E) of retailers meant the absence of Woolworths, Myer, David Jones, etc from our portfolios. These all performed poorly.

And our concern about the dividends, if they pay any, of many smaller mining stocks meant that we kept away (with one notable and successful exception) from what was a somewhat frothy sector.

So, where were our three main criteria met (and it can be one or more of the three)?

Cheapness (i.e. low P/E) meant that **Austar** (the regional pay TV company, average client return of +47%), **Aevum** (retirement village operator +84%) and **FerrAus** (small resources company +18%) were all subject to takeover offers.

**Australand** (+27%) was also cheap.

That is not to say that we buy companies because they might be subject to takeover. We buy them because they are cheap. And that cheapness is often recognised by other market companies rather than market investors.

Strong dividend growth (i.e. profit growth) was particularly found in **BHP** (average client return of +28%) and **RIO** (+30%).

Strong dividend growth and cheapness was found in **Emeco** (earthmoving equipment +103%); **Patties Foods** (makers of Four 'N Twenty Pies +59%); **Technology One** (enterprise software +30%); **Cardno** (engineering +38%) and **Challenger** (financial +38%).

We invest in companies for the long term. And it may take some time for the investment to be realised. And so we remain patient for such companies as **IAG** (-7%); **Tassal** (0%); **AMP** (0%); **QBE** (+2%); **Energy Developments** (+4%); **Primary Health** (+6%) and **AGL** (4%).

Each of these companies meets our criteria and we remain confident that in most cases our investment will be successful.

### ...and bad results...

As always, there is one company that disappoints more than any other. This year it was **Heemskirk**, which fell by over 50%.

Whilst the share price performance of Heemskirk has been disappointing this year, principally because of the Spanish tungsten operation not meeting expectations, the company has undergone a significant restructure.

This includes an agreement to sell the tungsten operations, and a new company Board.

Furthermore, the company has a sound balance sheet, and the future of the Canadian industrial minerals operations looks positive.

This is an investment with which we are prepared to be patient.



## INVESTMENT

# Significant transactions in the year

We are a low turnover investor. That means we are not active traders.

As we invest in a stock with a view to hold for at least three years, it follows that our portfolio turnover is less than 33% p.a. This compares to the market average of over 100%.

### Buys

Four companies were added to the equity portfolio during the year:

<b>Ausenco</b>	Ausenco is a consulting, engineering and project management services provider to the resource and energy sectors. It is set to benefit from a turnaround in activity following the GFC-related slowdown.
<b>Austar</b>	The pay TV provider for regional Australia (now subject to a takeover offer).
<b>IAG Insurance</b>	A general insurer principally operating in Australia, with NZ and UK businesses, see opposite.
<b>Trans-pacific Hybrids</b>	The hybrid securities issued by Transpacific (the diversified waste operator).

Not only does a low turnover approach reflect our focus on long-term investing, it also means avoidance of emotion-driven changes and also lower transaction costs.

And for those individual, trust or super portfolios that are taxable, clearly the opportunity for less CGT.

### Sales

This was balanced by the following sale transactions:

<b>Aevum</b>	Sold subsequent to a takeover offer from Stockland.
<b>Mermaid Marine</b>	Please see opposite page.
<b>Orica</b>	The mining explosives and chemical company was sold in Nov-10 on the basis that the company was considered fully valued. We elected to increase the cash position at the time, to allow us to participate in opportunities arising in subsequent months.
<b>Ramsay Health Care</b>	The global private hospital operator, was also sold in Nov-10, on the same basis as Orica (it was considered fully valued).

## Your other investments

### Property

Some of our clients have an asset allocation to “property”.

This asset class returned on average about 9% for our clients.

This allocation has the aim of providing income in conjunction with, over time, capital protection against inflation.

But we do not invest in real property. That is to say, you will not see us directly owning an office building in Bondi or a factory in Fremantle.

Our property investments are undertaken by investing in securities that have an interest in a range of properties. These securities are generally listed on the stock exchange and called listed property trusts, or, using the international term, Australian Real Estate Investment Trusts (A-REITs).

We select conservatively geared trusts (lower debt level), with sustainable distributions – paid from rental income received by the trust.

We remain cautious about this sector.

Good returns were received from **GPT** (average client return of 19%); **Challenger Diversified Property Group** (14%) and **Cromwell** (9%).

**Westfield's** performance disappointed (-8%).

### Income securities

Many clients invest in “income securities” or, as they are known by their traditional name, “fixed income.”

We also performed well in this sector, returning an average of about 10%, well above the benchmark.

Income securities is the better descriptor as these investments rarely have fixed income entitlements. The income stream generated is mostly “floating” rate i.e. one where the interest rate paid rises and falls at a pre-determined margin over a base rate. The base rate is often the bank bill rate. So as the bank bill rate changes, so too does the interest rate on the securities.

There are many income securities in which we invest, with performance generally even.

Some of the names are familiar, such as ANZ Convertible Preference Shares or IAG Notes.

But we also invest in less well known names where we are comfortable with the ability of the company to repay the debt. Some lesser known names include Orica Preference Securities and Ramsay Health Securities.

### International shares

We invest in international shares for diversification reasons. The diversification benefit comes about because of the lower correlation with Australian shares (principally caused by currency) and the expected long term return of the asset class.

It follows that we seek to capture the overall return from global share markets rather than to add value to global share markets.

These investments are unhedged, and so the total return captures both the movement in the Australian dollar as well as the movement in the international share markets.

In FY-11, the gain from rising world share markets (about 27%) was almost matched by the fall in value of those investments caused by the strength of the Australian dollar against a range of currencies (about 25%). Hence the final return was about 2%.

## Two investment snapshots

We set out below two investment snapshots, so as to give a flavour of some of our transactions.

### Mermaid Marine: taking profits

Mermaid Marine is Australia's largest marine services provider to the offshore oil and gas industry.

It has supply bases in Dampier and Broome, and a range of modern offshore vessels that principally operate in Australia (on the North West shelf).

Mermaid Marine was a stellar performer since the initial investment in May-08 and Sep-08, at an average purchase price of around \$1.56.

At various times since the initial purchase we have trimmed and "topped-up" the holding (depending on market movements), with a full sale of the remaining holding above \$3.00 in Feb-11 and Mar-11.

Mermaid Marine remains an excellent company; however, we considered that the market acknowledged this fact by virtue of its strong (\$3.00+) share price.

This price exceeded the valuation we ascribed to Mermaid Marine. Therefore, although we retained our favourable view of the company, we sold our entire holding during the financial year.

Mermaid Marine: taking profits



***"I enjoy working at First Samuel because our clients work closely with us, ensuring their financial needs are met. This level of co-operation is essential to our work, but it is hard to find elsewhere."***

*Jack Ngo, Associate Client Strategist, First Samuel*



### IAG Insurance: a contrarian view

Commencing in Jan-11, we added a new company to the equity allocation. At the time, and perhaps still today, some considered this a questionable move.

But that is the very opportunity. The market's negative reaction to insurance companies allowed us to acquire a good starting position in IAG in Jan-11, which we have subsequently increased.

IAG has a strong portfolio of insurance brands and joint venture arrangements across Australia and NZ (including CGU and NRMA), remediation of its UK operation is underway, and it has a strong balance sheet.

IAG is now concluding its third year of a turnaround process, and is on the cusp of delivering some significant increases in its profit level – even after the impact of the Queensland floods and other natural disasters.

Furthermore at the latest strategy day, the company confirmed it is now able to shift its focus to growth.

IAG is now well managed, and we expect further improvements in profitability over the coming years.

It takes time and patience to see change in insurance businesses, something the market typically doesn't have – hence this opportunity.

We anticipate strong dividend growth, and on our estimates of IAG's FY-11 profit, it is trading on a P/E of around 12, compared to a historical average of 14.5.

## INVESTMENT

# How your share portfolio is structured going into FY-12

### A reminder of how we invest

The reality is that investment management is complex. Which is why self-management is not viable.

But for convenience we have distilled what we do into a number of key elements:

1. Heads I win, tails I don't lose too much ("asymmetry"). We will make mistakes, so protect the downside.
2. Just focus on what we can understand. There is no point in making guesses about a company. If we cannot understand it, we do not invest.
3. Look to three year returns. If you think longer term, you will not be spooked by short term volatility (and hence making decisions based on emotions, rather than longer-term fundamentals).
4. Only own what we like. Decisions based on index weights (i.e. size) are, well, stupid. Why own something you do not like?

We then overlay our search with the three individual stock characteristics:

- predictable and strong dividends;
- growing dividends (because of growing profits; and
- cheap (generally as measured by P/E).

### Growing dividends that are cheap

The average client's share portfolio has a **dividend yield** of about 5%. This is just a little higher than the market (this is good).

And we expect those **dividends to increase** by about 13% p.a. over the next three years. That is to say we expect profits (or "earnings") to grow at that rate.

In terms of "value" it has a very **low P/E** of about 9.4. That is to say, it is cheap.

And so we consider your share portfolio to be well placed to benefit as the market recovers.

*"I make a difference for our clients by professionally dealing with all aspects of their Super Fund administration... which means they don't have to!"*

Emma Coote, Controller Investments and Finance,  
First Samuel

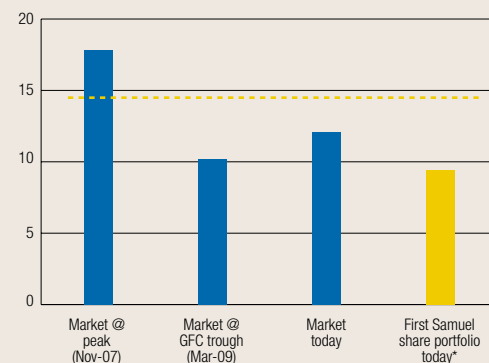
The good yield is a reminder of the importance of income. And mostly the income steadily grows, regardless of the share price.

Providing that people:

- keep eating pies (Patties)
- keep buying salmon (Tassal)
- need electricity (Origin, AGL, Energy Developments)
- need the doctor (Primary)
- need to insure themselves (QBE, IAG, AMP)
- need a number of other core goods and services

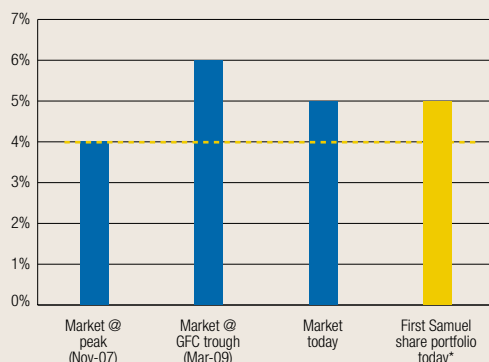
we expect that this current year-end nervousness will have very little real impact on the dividends you receive and the growth in those dividends.

### Entering FY-12 with a "cheap"\* share portfolio...



\* As measured by P/E. A low P/E is good, – see text. "Today" is 30-Jun-11

### ...that also has a good yield



\* As measured by P/E. A low P/E is good, – see text. "Today" is 30-Jun-11

# Administration & reporting – what we did for our clients

Our service does not end with the strategy we give or the investment returns we provide. It is ongoing.

## Client services

Here are some of the things we did for our clients over the past 12 months:

### CIO Conversations

These are small, round table dinners, held in suburbs where our clients live. The “conversation” is with Dennison Hambling, our Chief Investment Officer, and with other First Samuel Associates.

It provides the opportunity for our clients to discuss their investments, the economy and the markets in a relaxed, friendly environment.

### Annual Forum

This is our large annual event, held in Melbourne. We have a guest speaker whom we believe provides an interesting and informative presentation on a subject relating to wealth management.

Previous speakers have included:

Hon. Peter Costello, former Treasurer of the Commonwealth of Australia; Saul Eslake, former Chief Economist, ANZ Banking Group and Professor Ian Harper, former Head of Australian Fair Pay Commission.

### Eat Street

Our annual charity event is held at the Sofitel in Melbourne. This food and wine fest allows clients, as our guests, to stroll amongst booths and sample wares from some of Melbourne’s finest restaurants and Victoria’s leading wineries.

First Samuel is a major sponsor of this event, the entire proceeds of which go to charity.

### Seminars

Some of our clients are keen to introduce their colleagues or friends to us. To facilitate an easy introduction we hold a series of seminars, where our key Associates give presentations on aspects of our service.

### Wry & Dry

Wry & Dry is our weekly client email. It provides a cynical view of the week’s wealth management events.

### Quarterly reports

Quarterly, a formal report is provided to each client. The Report shows their investments, their performance and other key matters.

### Accountant’s Pack

Annually, each client receives a comprehensive pack of information for use by their accountant in the preparation of the necessary taxation and other returns.

### Independent audit certificate

Annually, every client receives an audit certificate on their individual portfolios, provided by an independent firm of auditors.

### Formal reviews of your investments

Monthly, we formally review each client’s investment portfolio.

### Review of your Investment Programme

At least annually, we formally review the Investment Programme that each client has for each portfolio, to ensure that the Programme still meets each client’s needs.

### Annual Investment Report

Annually, each client receives a comprehensive, hard copy report on their investments.

### Daily

Every morning, before 10am, five reports on each client’s portfolios are uploaded onto that client’s secure page on our website, for electronic access (with a password & PIN). Archives of previous Quarterly and Annual Reports and Accountant’s Packs are also accessible.



## YOUR FIRST SAMUEL TEAM



*“The provision of individual, indispensable and enduring relationships that create manage and protect wealth”*

### Directors

Murray Philip Baird BA, LLB, MAICD - Chairman  
John Alexander Bryson B.Eng (Mech), MBA, MAICD  
Antony Baron Greenwood LLB, FAIM, MAICD  
Elizabeth Henty Parkin B.Bus, FFin, ACA MAICD  
Anthony Hamilton Tom Starkins LLB, B.Ec, CFA, FFin, MAICD

### General Manager

Joseph Anthony Flinn, B.Acc, CA

### Company Secretary

Timothy Watkinson, Watkinson Legal  
Joseph Anthony Flinn, B.Acc, CA

### Counsel

Watkinson Legal

### Auditors

MSI Ragg Weir & Co

### Registered Office

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*Left to right: Craig Fraser, Nikki Hill, Dennison Hambling, Susanne Retallick, Jack Ngo, Fleur Graves, Anthony Starkins, Duro Rudic, Emma Coote, Kelly White, Roy Leech, Zoë Borg, Joe Flinn, Jenny Forbes, Cameron Blackwell, Simon Devlin*

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***“The Lord declares those who honour me I shall also honour”***

*From the First Book of Samuel, chapter 2, verse 30*

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Live well. Sleep well.