Conscious Investor Fund
Annual Letter to Members: 2013 -2014

Your Capital Allocation Team has been busy looking for secure investments for your money. Our role has three parts:

- Identifying great businesses in which we have confidence that earnings will continue to grow
- Ensuring that management is trustworthy and acting in the best interests of shareholders
- Buying at a price that offers a reasonable return with safety

For each company that meets these criteria we set a range of prices that we believe would result in at least a satisfactory return. Mostly the companies have been at the high end of this range. This means that as investments came into the fund, usually it was a matter of buying small parcels to try to take advantage of dips in prices. This has been much easier since we changed to Interactive Brokers (although the changeover involved considerable paperwork). It is also been much cheaper. For example, the fee for a $12,500 trade is only $10.

Warren Buffett in His Own Words

Every investor knows about Warren Buffett. His investment record since 1962 is unparalleled. He bought his first shares in Berkshire Hathaway on 12 December of that year for US$7.50 quickly accumulating a majority holding. Today those same shares are worth an eye-watering US$194,000 each.

Not so many know that during that period on four separate occasions the share price of Berkshire Hathaway has dropped by over 50 percent from its previous high point. Each time, as John Price writes in *The Conscious Investor*, it picked itself off the canvas and headed for record highs. For example, on 19 September 2008, Berkshire Hathaway A shares (BRK.A) reached a price of US$147,000. Less than six months later on 5 March 2009, they dropped to US$73,370. Now, of course, they are at record highs almost reaching the US$200,000 mark.

There are many opinions about the reasons for Buffett's success. Let's look at his own words writing in his letter to shareholders in 1995:

> Your goal as an investor should simply be to purchase, at a rational price, a part interest in an easily-understandable business whose earnings are virtually certain to be materially higher five, ten and twenty years from now… Put together a portfolio of companies whose aggregate earnings march upward over the years, and so also will the portfolio's market value.
>
> Though it's seldom recognized, this is the exact approach that has produced gains for Berkshire shareholders: Our … earnings have grown at a good clip over the years, and our stock price has risen correspondingly.
>
> Had those gains in earnings not materialized, there would have been little increase in Berkshire's value.

If this is not enough, every year for 40 years he has written in the annual report of Berkshire Hathaway that he is only interested in companies with "demonstrated consistent earning power". This is why fr the Fund we continue to look for companies with high stability of past earnings as well as all the hallmarks that this growth will continue into the future. This means such things as low debt, consistent return on equity and clear economic moats. It also means management that are honest, rational and acting in the best interests of shareholders.

Berkshire Hathaway Annual Meeting

Attending the annual meeting of Berkshire Hathaway, often dubbed the Woodstock for Capitalists, is a unique experience. Over recent years the number of attendees has ballooned to over 30,000. Most of the meeting consists of a Q&A with Warren Buffett and Charlie Munger. Not so many know that downstairs from the meeting is a giant expo with booths run by many of the companies that Berkshire Hathaway owns or has a major shareholding. The booths range from Acme Brick Company to Clayton Homes to Dairy Queen to NetJets to World Book.

Attendees can buy items from many of these booths ranging from Cowboy boots at the Justin Brand booth to boxer shorts emblazoned with Buffett and Munger's caricatures at the Fruit of the Loom booth. The more well-heeled investors can become a fractional owner of a Gulfstream G550 (price on application!) from NetJets or buy luxury watches such as Jaegre LeCoultre for $100,000 and more from Borsheim's.

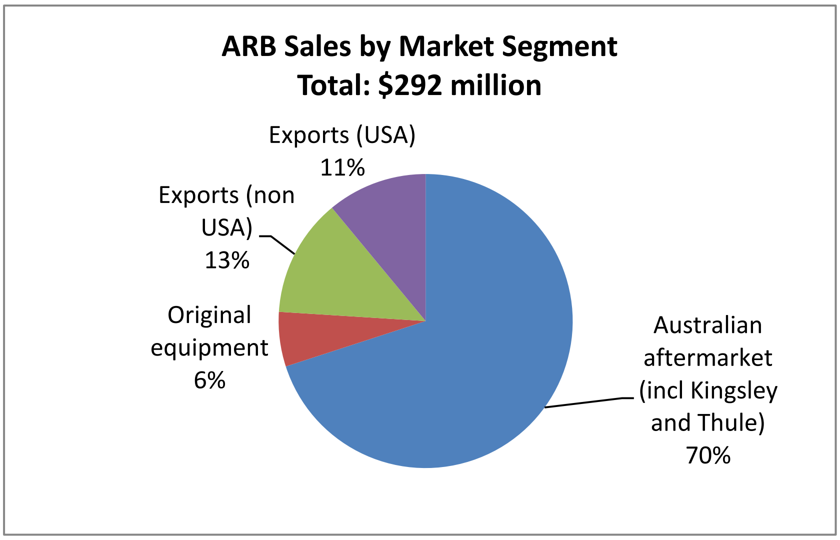
Even though the annual meeting of Berkshire Hathaway is a lot of fun, particularly the expo of the BH companies, Buffett takes the opportunity of displaying and promoting the portfolio of BH companies very seriously. Although it is early days, your Capital Allocation Team also takes very seriously the goal of using your money wisely to build a portfolio of outstanding businesses, a mini Berkshire Hathaway.

A Mini Berkshire Hathaway

Let's look at the largest ten holdings in the Fund. These would form a wonderful core for any exhibition of quality companies. They cover a broad range of industries (including automotive supplies, banking, sporting goods, travel, pharmaceuticals and health care), geographical location (some are just in Australia and others are truly global companies), and market capitalisation (ranging from $826 million for ARB to $111 billion for the Commonwealth Bank). What they have in common is a proven record of growth in earnings and sales, strong economic moats, and management that understands and respects the ownership of shareholders.

ARB Corporation (symbol ARP)

ARB is a great Australian success story. In 1975 company founder, Tony Brown, completed a 4WD trip through the top end of Australia. Back then, 4WDers relied on homemade or ill-fitting equipment that was not designed for extensive Outback expeditions. Endless corrugated roads, extreme temperatures, and the heavy loads carried by Australian travellers were extremely punishing on vehicles that regularly tackled these kinds of conditions.



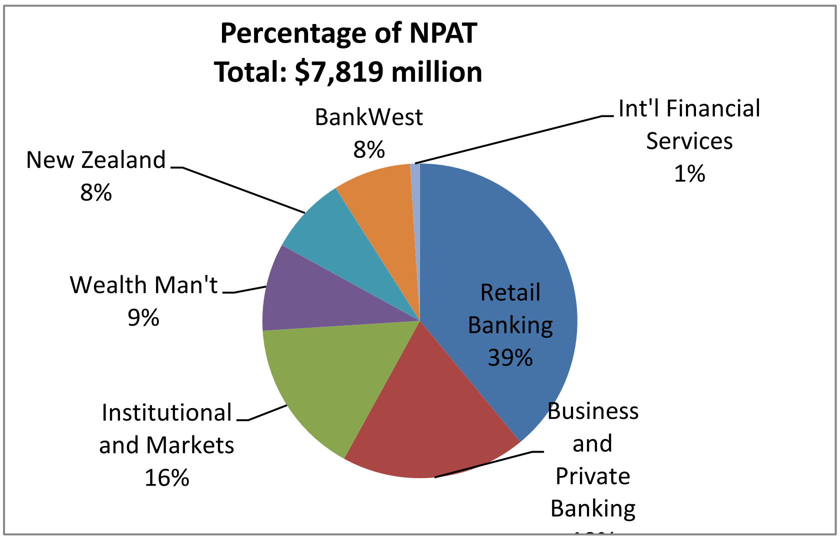
Upon his return to Melbourne, Tony began working in the family garage to address some of the product deficiencies he had encountered on his trip. It was exactly what Australian 4WDers had been waiting for, and ARB, the initials of Anthony Ronald Brown, was founded.

Today, ARB is Australia's largest manufacturer and distributor of 4x4 accessories. We also have an international presence, with an office in the USA and an export network that extends through more than 100 countries around the globe.

From a business perspective, annual earnings per share have grown from 2.8 cents in 1994 to 57.4 cents today.

Commonwealth Bank (symbol: CBA)

The Commonwealth Bank was founded under the Commonwealth Bank Act in 1911 and commenced operations in 1912 as both a savings and general banking business. In July 2012 CBA celebrated the centenary of the opening of its first branch in Collins Street, Melbourne on 15 July 1912. Today CBA is a business with more than 800,000 shareholders and 52,000 employees. The bank offers a full range of financial services to help customers build and manage their finances.

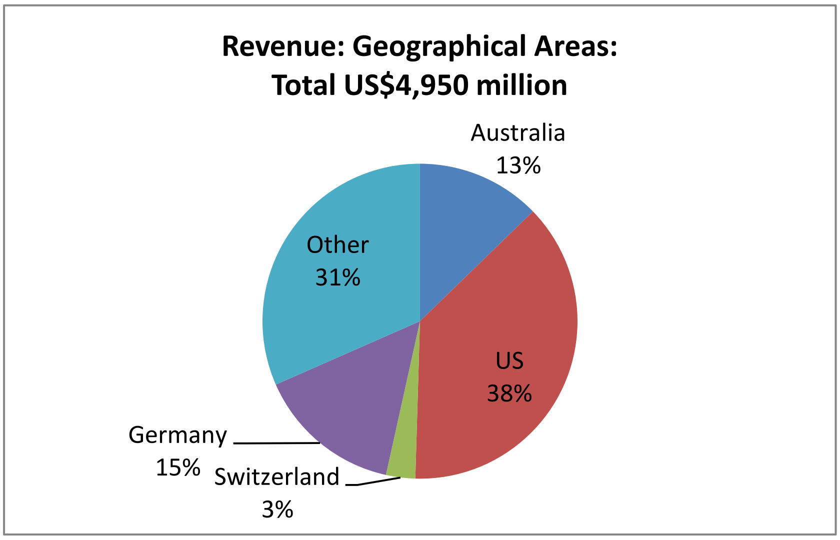


Today CBA has branches in Indonesia, Japan, Singapore, India, Vietnam, Mainland China and SAR Hong Kong. It also has representative offices in Beijing, and Hanoi. Other branches are in the United Kingdom, New Zealand the US.

Annual earnings per share have grown from $1.97 in 2004 to $5.18 today.

CSL Limited (Symbol: CSL)

The Commonwealth Serum Laboratories was established in Australia in 1916 to service the health needs of a nation isolated by war. CSL Limited was then incorporated in 1991 and listed on the ASX in 1994. Since then CSL acquired a number of businesses including CSL Behring. CSL Behring can trace its corporate roots back to Emil von Behring, an innovator with serum therapies who won the first Nobel Prize in Physiology and Medicine. CSL (including CSL Behring) produces a range of life-saving products with particular focus on vaccines for the prevention and treatment of serious disease.



CSL Behring is a leader in the plasma protein therapeutics industry. Its products are produced at facilities in Bern, Switzerland; Marburg, Germany; Kankakee, Illinois and Broadmeadows, Australia, in accordance with international safety and quality standards. Additionally, CSL Behring operates one of the world's largest plasma collection networks, CSL Plasma, with over 400,000 donors worldwide. CSL Behring provides 98 percent of the EBITDA.

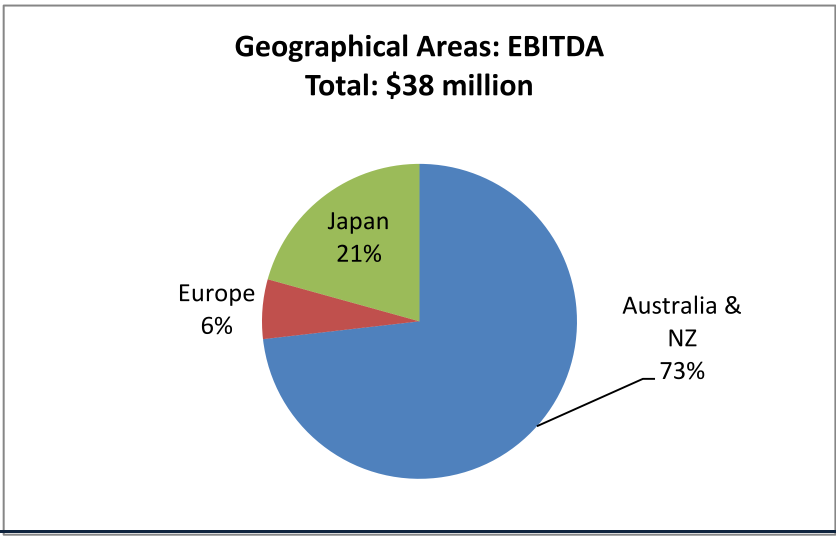
Another division of CSL is bioCSL, which manufactures and markets biological products for human use, in-licenses and markets vaccines and prescription pharmaceuticals to treat a range of human medical conditions as well as manufactures and markets in vitro diagnostic products.

The company has major facilities in Australia, Germany, Switzerland and the U.S. with over 10,000 employees working in 27 countries.

Annual earnings per share have grown from 14.1 cents in 2004 to $2.91 today.

Domino’s Pizza (Symbol: DMP)

Domino's Pizza Enterprises Ltd (Domino's Pizza) is the largest pizza chain in Australia in terms of both network store numbers and network sales. It is also the largest franchisee for the Domino's Pizza brand in the world. The company holds the exclusive master franchise rights for the Domino's brand and network in Australia, New Zealand, France, Belgium, the



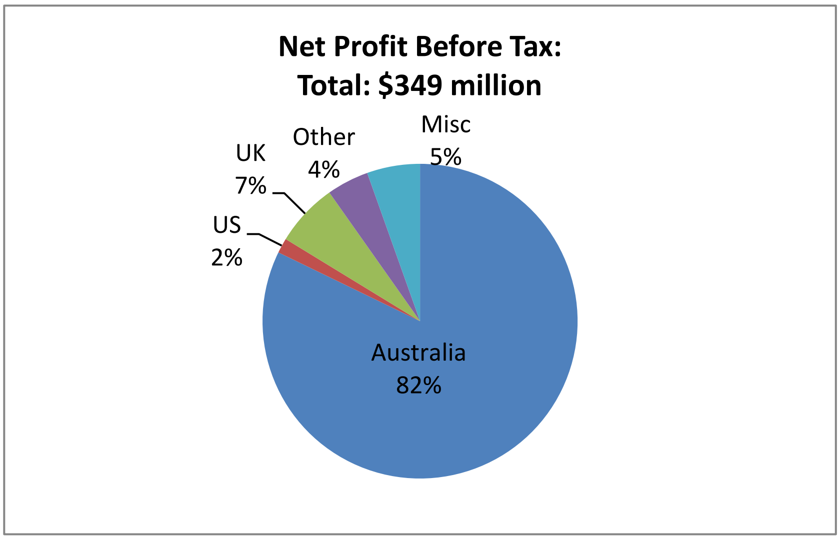
Netherlands, the Principality of Monaco and Japan. With more than 1300 stores, it employs approximately 26,000.

The strength of Domino's lies in its ability to use different apps and web sites to facilitate the ordering process. Australian online sales are at the 57 percent level. Recently the company added the ability to design and name your own pizza. You can then promote it via your own mailing lists and social media earning a small commission on each sale.

Annual earnings per share have grown from 13.3 cents in 2005 to 47.0 cents today. Currently return on equity is 29.7 percent.

Flight Centre Travel (Symbol: FLT)

After starting with one shop in the early 1980s, Flight Centre has grown to become a $13.5 billion business consisting of more than 30 brands. One of the world's largest travel agency groups, it has company-owned operations in Australia, New Zealand, the United States, Canada, the United Kingdom, South Africa, India, China, Hong Kong, Singapore and the United Arab Emirates. Its travel management network spans more than 75 countries. It employs more than 15,000 people globally and has 2,500 stores.



According to the company, its vision is: "To be the world's most exciting travel company, delivering an amazing experience to our people, customers and partners."

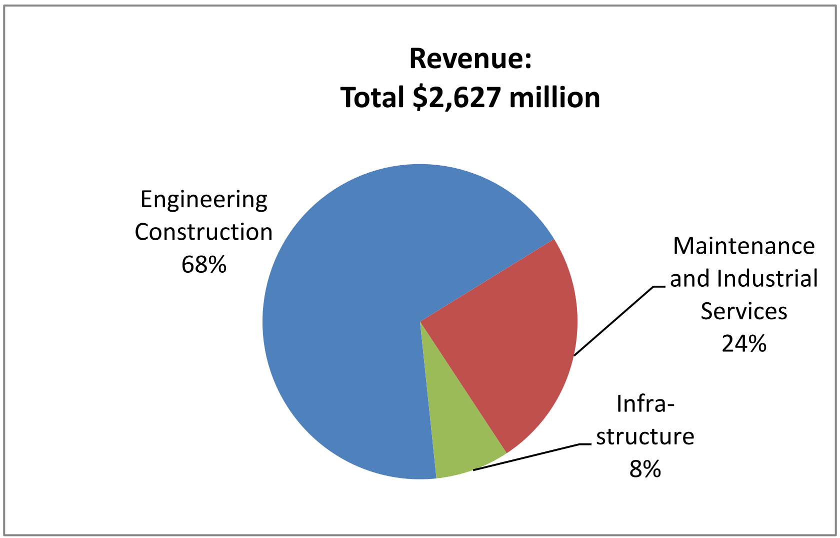
Its basic operating mode is through small neighbourhood stores with between 3 and 7 staff called families. Between 3 and 7 families make up a village, and so on up to the level of the global executive team.

Flight Centre was a late starter in the area of online travel agents and online travel booking preferring to focus on the more conventional store front. However, it now has an attractive online booking system. The stated goal of the company is to have a blended system bringing together the best of store and online booking and service.

Annual earnings per share have grown from 89.4 cents in 2004 to $2.63 today.

Monadelphous Group (Symbol: MND)

Monadelphous is a leading Australian engineering group providing construction, maintenance and industrial services to the resources, energy and infrastructure sectors. It is involved in some of Australia's biggest and most complex projects and facilities. The company prides itself on producing solid, quality work, maintaining a clear customer focus and providing safe, reliable, innovative and cost-effective service solutions.



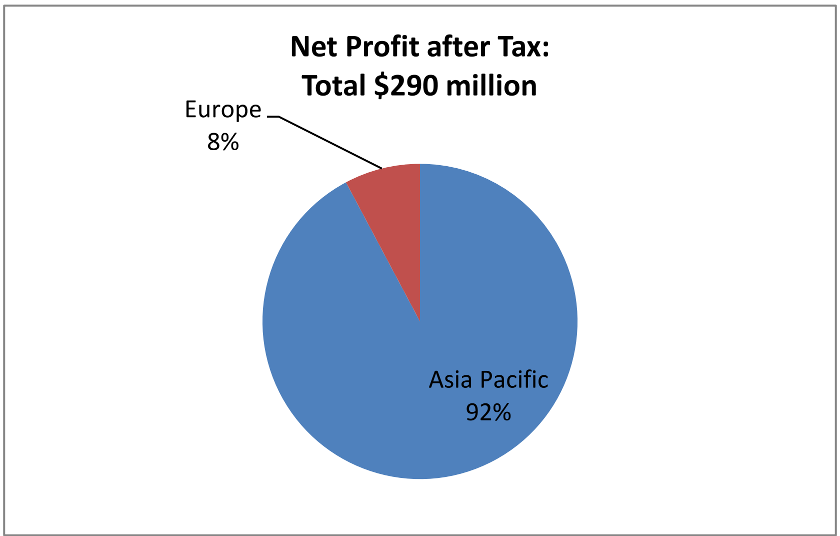
MND employs more than 7000 people, with major offices in Perth, Western Australia, and Brisbane, Queensland, supporting its operations in projects, facilities and workshops spread across Australia and in neighbouring countries including Papua New Guinea and China.

Recent major contracts include a construction contract for mechanical works at the Ichthys Project Onshore LNG Facilities in Darwin in the Northern Territory (February 2014;$680 million) and an iron ore construction project with Sino Iron Pty Ltd at the Sino Iron Project, located at Cape Preston, near Karratha in Western Australia (July 2014; $160 million). In February, the company said that it was in a strong position to secure new contracts in both upstream and downstream LNG projects.

Annual earnings per share have grown from 10.9 cents in 2004 to $1.70 today.

Ramsay Health Care (Symbol: RHC)

Ramsay Health Care is a provider of private healthcare in the UK, Australia, France, Indonesia and Malaysia. Established in Sydney, Australia in 1964, the company specialises in surgery, rehabilitation and psychiatric care. Its growth has been driven by demographics and continuous business improvement, brownfield developments, new partnerships with public and private operators, and exploring further acquisitions.



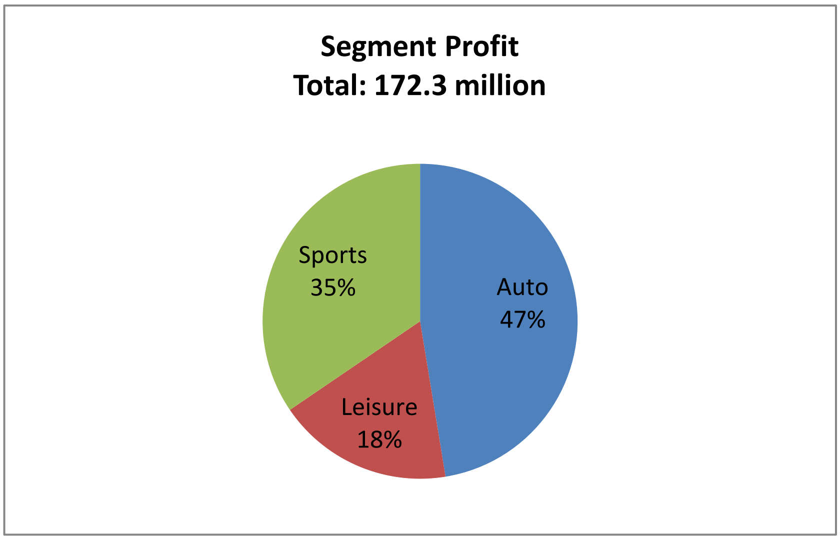
Even though its debt is higher than we usually like, because it is mostly in the form of land and buildings (hospitals), the Capital Allocation Team are happy to have it in the portfolio.

The most recent acquisition is joint with Crédit Agricole Assurances to purchase 83.43 percent of Générale de Santé. The cost to RHC is approximately $627 million. It consists of 75 facilities (including 61 hospitals) in the fields of medicine, surgery, obstetrics and rehabilitation. It employs around 19,000 staff. This brings Ramsay's total portfolio in France to 115 facilities (including 101 hospitals) and 15,400 beds.

Annual earnings per share have grown from 32.6 cents in 2004 to $1.46 today.

Super Retail Group (Symbol: SUL)

Super Retail Group Limited is a specialty retailer with retail network spanning three main retail divisions: Auto, Leisure and Sports, with 7 retail brands. In addition, SUL has retail network located in New Zealand, and has international operations and sourcing presence extending into Asia and across India.



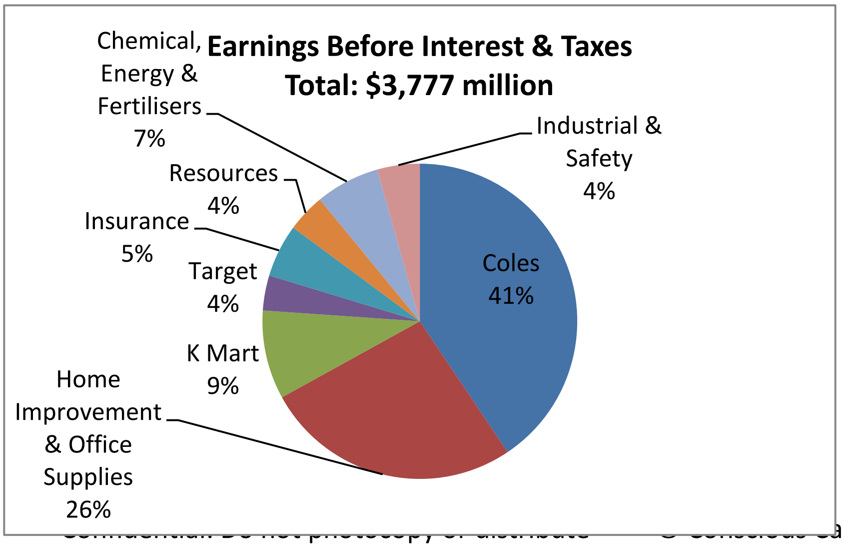
Generally SUL stores have a warehouse structure stocking over 10,000 products predominantly priced at the lower end of the market with an offer to beat any price. A rising proportion of house-brands helps reduce the cost of goods and boost margins. New stores are opening at a rate of roughly 30 per annum.

Recently the company has put a lot of attention and spent a lot of money on logistics and supply chain refinement. For instance, in the last four years, the IT staff has doubled in size from 35 to 70. It has made the transition from a 24-hour core systems and website update schedule to a near real-time, true multi-channel operation.

Its brands are Amart Sports, BCF (Boating Fishing Camping), FCO (Fishing, Camping Outdoors), Goldcross Cycles, Supercheap Auto, Rays Outdoors, Rebel Sports and Workout World.

Annual earnings per share have grown from 24.6 cents in 2004 to 59.2 cents today.

Wesfarmers Limited (Symbol: WES)



Wesfarmers is best known as the owner and operator of Coles Supermarkets. However, the company is really a conglomerate which buys and sells its component companies at suitable times. For example, in June 2014 Wesfarmers completed the sale of its insurance broking and premium funding operations to Arthur J. Gallagher & Co for a pre-tax profit of approximately $310 to $355 million. Later that month it announced the completion of the sale of its insurance underwriting operations to Insurance Australia Group for a pre-tax profit of approximately $700 million to $750 million.

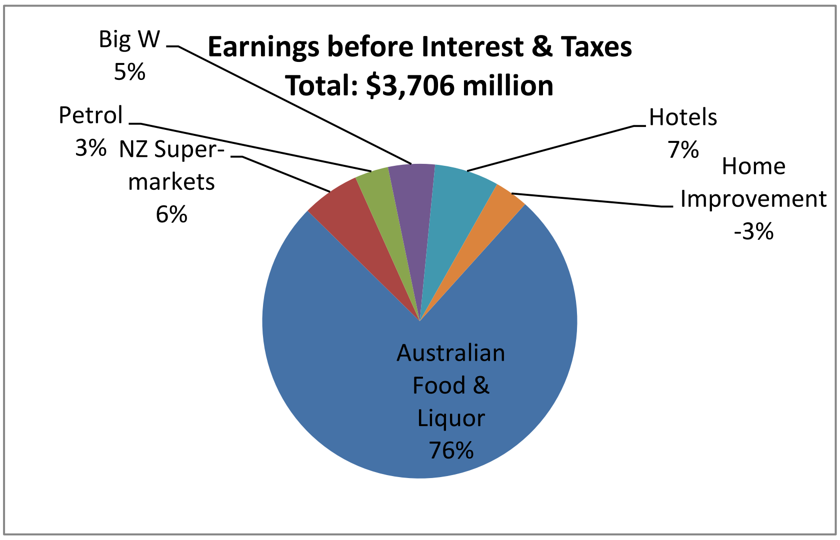
Apart from Coles, the company covers the areas of home improvement (Bunnings), office supplies (Officeworks), department store retailer (Kmart and Target), Resources (open cut coal in Curragh and Bengalla), chemical, energy & fertilisers (mainly ammonia and ammonium nitrate production in Western Australia and Queensland) and industrial & safety. (Insurance is no longer part of Wesfarmers group of companies. Coles now offers home, car and life insurance.

The pie chart shows the breakdown of earnings before interest and taxes for the financial year ending June 2013.

It is generally felt that Wesfarmers paid too much for Coles when it acquired it on 23 November 2007 for $22 billion. For example, before the purchase EPS was as high as $2.18 for FY06. They are now only back to $2.09. However, they have grown by an average of 12.4 percent per year for the past three years.

Woolworths Limited (Symbol: WOW)

Since opening its first single basement store in Sydney's Pitt Street in 1924, Woolworths now has a store in almost every metropolitan and regional centre in Australia and New Zealand. The company stared operating fresh food stores 60 years ago when advances in refrigeration technology revolutionised transport and storage.



Other brands of Woolworths are Big W, BWS, Dan Murphy's, Woolworths Mobile Wine Market, Cellarmasters, Langton's, Masters Home Improvement and Thomas Dux. Similarly to Coles, the company now offers home, car and life insurance. It also offers travel and pet insurance.

In partnership with Lowe's USA) in 2011 Woolworths started a new chain of hardware stores called Masters. To date they are still losing money. For FY13 they lost 138.9 million and there is some suggestion that it will be a few more years before they are profitable.

The Capital Allocation Team thought that, since probably less than 1 percent of Woolworths' revenue comes from poker machines, it was acceptable for the Fund.

Annual earnings per share have grown from 66.6 cents in 2004 to $1.88 today.

Role and Performance of Largest Holdings

The Conscious capital Fund is a boutique fund that will remain small and true to its principles rather than include companies that do not satisfy its stringent requirements. The recommended time frame for investing in the Fund is 5 years or more to allow for the future success of the companies held by the Fund to be reflected in share prices and dividends.

The companies just described make up the core ten of the Fund. No businesses stay the same. Yet we feel that these businesses are such that they will be very similar in five and ten years' time but with greatly expanded sales and earnings.

The Capital Allocation Team decided that these companies could make up to around 60 percent of the fund. Currently they are at the 58.3 percent level.

The following table shows the average eps growth over the past five years, the dividend yield, total outlay for each of the companies and the total value at the end of June as measured by the market value and cash dividends over the holding periods of this core ten.

Shares	Name	EPS Growth 5 Yrs	Div Yld (1)	Total Outlay (2)	Value 30 June 2014 (3)
23,000	Domino's Pizza	19.20%	1.6%	$265,748	$526,139
55,000	Super Retail	19.85%	3.9%	$591,178	$506,137
10,600	Flight Centre Travel	15.30%	3.1%	$505,639	$501,735
28,000	Monadelphous Group	17.08%	8.1%	$490,401	$490,328
10,000	Ramsay Health Care	17.21%	1.6%	$431,856	$462,965
10,400	Wesfarmers Limited	3.18%	4.4%	$435,917	$451,367
6,500	CSL Limited	11.80%	1.8%	$445,892	$446,722
36,000	ARB Corporation	15.06%	2.3%	$416,560	$446,341
11,800	Woolworths Limited	8.99%	3.7%	$411,128	$440,497
5,000	Commonwealth Bank	8.02%	4.6%	$377,407	$414,960
	Subtotal			$4,371,726	$4,687,191
	Other Companies			$2,818,171	$2,492,293
	Total			$7,189,897	$7,179,484

(1) The dividend yield assumes that the shares were held for a full 12 months.
(2) The Total Outlay is the total amount paid for the position in each company starting in March 2013 up to the end of June 2014.
(3) The Value column includes receipts from cash dividends over the lives of the holdings. The dividends do not include franking credits.

The average dividend yield for these companies is 3.5 percent. However, at this stage when positions are still being built, the actual dividends received by the Fund were usually less. From the dividends received by the Fund, to date the Fund has distributed $196,719 to members as gross dividends consisting of cash, franking credits and foreign tax credits. With expected earnings growth in the upcoming reporting season, we should start to see a less patchy and growing quantum of dividends with accompanying franking credits.

Over the last six months we have taken what opportunities we can to build the holdings of our core 10 businesses. In time we anticipate capital and dividend growth through the increases in earnings.

War Chest

As at the end of June 2014 we held 9.42 percent of our portfolio in cash. While the returns on cash are low, we view this as a war chest we have ready to deploy the moment Mr Market falls out of love with one of our favourite companies – as we can expect to happen from time to time. While this may cause other investors to panic, we're overjoyed when we see great businesses sold down to bargain prices. Your Capital Investment Team stands ready to act quickly to deploy cash when Mr Market obliges.

Conscious Investor® and the Teaminvest Methodology

The investment process used by the Capital Allocation Team for the Fund consists of four steps: Filtering using Conscious Investor®; Applying the Teaminvest investment methodology; Calculating the price to pay and when to sell; and a Final Checklist. Full details of these steps are contained in the Information Memorandum. Here we just give a brief summary of the first two steps.

Conscious Investor® filters and analyses all companies listed on the ASX in three steps: Filter, Research and Return. The main components of the filter stage zero in on companies with attributes such as strong and stable growth in earnings and sales, high and consistent return on equity and not too much debt. The research stage helps to limit the results to companies for which these attributes are likely to continue. Finally, the return stage calculates what maximum price to pay to be confident about getting the required rate of return over the long term. It uses automatic margin-of-safety calculations based on stress testing the investment assumptions.

The Teaminvest Methodology focuses on the following four areas. Wherever possible the Capital Allocation Team scores the areas to increase the precision of the decision process.

- How does the company make money? What is the business of the company? Who are its customers?
- Investments should be like castles with deep moats: What are unique features of the business that separate it from its competitors? These "economic moats" are scored in terms of depth and durability.
- Risks need to be identified: All businesses face risks that could weaken the continuing success of their operations. These risks are identified and are scored according to the likelihood of their occurring over the next economic cycle and their potential damage if they do.
- Is management honest, open and rational? As part of examining the business, evaluation is made whether or not it is believed that the board and senior management are acting honestly, rationally and in the best interests of shareholders. Specific areas that are looked

at include the number and type of related party transactions and the remuneration structure for the CEO and senior management. The Capital Allocation Team scores remuneration in terms of clarity, alignment and quantum.

The Capital Allocation Team prepared this report for members of the Conscious Investor® Fund. It does not take into account anyone's personal circumstances. Remember, what happened in the past is not always what will happen in the future.

Questions? Contact us:

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