

AUSTRALIAN ENHANCED INCOME FUND

Appendix 4E

Half Year Report

For the Year ended 30 June 2009

Results for announcement to the market
All comparisons to the year ended 30 June 2008

Revenue & Profit	Change from previous period	Year to 30 June 2009	Year to 30/6/2008
Revenue from ordinary activities	(36%)	1,732,115	2,689,784
Profit from ordinary activities after tax attributable to members	(8%)	(5,107,269)	(4,739,901)
Net profit for period attributable to unit holders	(8%)	(5,107,269)	(4,739,901)

Distributions	Year to 30/6/2009	
September quarter distribution	17.5 cents	
December quarter distribution	17.5 cents	
March quarter distribution	17.5 cents	
June quarter distribution	17.5 cents	

June quarter distribution details	Year to 30/6/2009	
Record date for distribution	30/06/2009	
Payment date for distribution	17/7/09	
Estimated franking	28%	
Price of units issued under DRP	\$5.375	

Distributions for the Year ending 30 June 2009 were paid in accordance with the Product Disclosure statement (PDS) which states that the fund will make distributions at a minimum rate of 7% per annum.

The Distribution Reinvestment Plan (DRP) was in operation for the Final Distribution of 17.5 cents per unit. Participating unitholders were entitled to be allotted the number of units (rounded to the nearest whole number) which the cash distribution would purchase at the relevant issue price. Unitholders wishing to participate in the DRP must have informed Registries Ltd of their intention to do so by 30 June 2009 (the record date). Units issued as part of the DRP were issued at \$5.375

	Year to 30/6/2009	Year to 30/6/2008
Net Asset Value	\$5.626	\$7.75
Closing Unit Price (on market)	\$5.55	\$8.00

This report is based on the financial report which is in the process of being audited.

Market and Performance Review

Hybrid Markets

Credit markets, as with all investment markets, suffered an annus horribulus in 2008/2009. At one stage in March 2009 hybrid markets had fallen 24% since the start of the financial year. Markets recovered during the June quarter and the recovery has continued into this financial year with the hybrid sector around 6% higher since June 30.

The basis for the weakness was the collapse of the bubble in the US property market, where both residential and commercial property prices increased rapidly over the middle years of this decade. This was financed by an enormous increase in leverage both in and outside the banking sector. When the bubble collapsed, it resulted in what some commentators refer to as the Banking Panic with the consequence that the entire UK banking sector and large portions of the European and US sectors collapsed. As banks had to shed assets into a market with limited buying, prices of credit investments fell to levels not seen since the Great Depression. The combination of a failing banking system and collapsing US house prices pushed most global economies into severe recessions. Australia was always only ever going to enter a shallow recession and it now seems that it will not even be that

Despite the benign economic conditions, hybrid markets in Australia were even more badly affected than offshore due to a large amount of margin loan and fund related selling into a market with even fewer buyers.

The Australian Enhanced Income Fund was not immune to events and the NAV performed poorly due to its holdings of non bank securities, which were most affected by the crisis. The large proportion of the losses are unrealized and reflect the fall in prices of hybrids from the circa \$100 level that is normal to the circa \$70 level at 30 June.

Income levels fell in line with the falling bank bill rate, but the fund maintained its 7% p.a. distribution rate for the year. Distributions for upcoming periods will be reduced to 5%. The benefit of franking for the year was equivalent to 0.9%.

Outlook

The year has started off brightly for both the Fund and the hybrid market. The NAV of the Fund has increased 13% between 30 June and 10 August.

In many ways the increase in market prices has been the exact opposite of events on the way down. It has occurred on very thin volume and, often, with little rationality. Nevertheless, the market remains extremely cheap, both in historical terms and relative to other credit markets. We expect that hybrid prices will continue to revert towards \$100, some quicker than others, and for volatility to decrease as securities approach \$100.

Markets are anticipating an increase in cash rates which will increase the income due to the largely floating rate nature of the investments. Currently the expected level of cash rates in March 2010 is over 4%, a material increase. This will flow through to income as cash rates rise.

If, as seems likely, the slowdown is over or close to over, it has traditionally been an excellent time to invest in credit. Unlike equities which take some time for earnings to recover, credit investments benefit from the removal of 2 of the enormous headwinds which have affected markets over the past 2 years. Default activity falls dramatically as economies recover from recession as the survivors are stronger and banks are less likely to call in loans. In addition credit margins, which are still at what are unprecedented levels, tend to fall towards historical averages. There is no better time to invest in credit than at the end of a recession. Historically, credit markets have outperformed equity markets until about 3 years into a recovery.

Fund Structure

The table details the top 10 holdings and yields and prices as at 30 June 2009. It shows the discounts, yields and prices available on hybrids issued by good quality companies

Security	Holding	Yield	Price
Macquarie Airports FLYERS (MAZPA)	10.5%	9.4%	103.55
Bendigo Bank Reset Pref (BENPA)	8.1%	10.5%	97.49
Orica SPS (ORIPB)	7.8%	10.3%	90.45
AXA Subordinated Notes (AXJHA)	6.9%	13.2%	50.60
IAG Reset Pref (IAGPA)	6.5%	8.7%	100.5
Multiplex SITES (MXUPA)	5.5%	22.3%	39.25
Australand ASSETS (AAZPB)	4.8%	21.8%	58.00
Gunns FORESTS (GNSPA)	3.9%	20.1%	61.00
Nufarm Step Up Securities (NFNG)	3.6%	17.1%	73.90
Skycity ACES (SKAG)	3.2%	10.4%	91.50

AUSTRALIAN ENHANCED INCOME FUND
ARSN 115 632 990
INCOME STATEMENT
FOR THE YEAR ENDED 30 June 2009

	Notes	June 2009 \$	June 2008 \$
Revenue	2	1,732,115	2,689,784
Management Fees		(160,801)	(232,380)
Fund Expenses		(128,243)	(129,626)
Finance costs		(49,396)	(156,793)
Net loss on financial assets held at fair value through profit and loss		(6,501,213)	(6,910,886)
Profit attributable to unitholders before income tax		<u>(5,107,538)</u>	<u>(4,739,901)</u>
Income tax expense	1(a)	-	-
Profit attributable to unitholders		<u>(5,107,538)</u>	<u>(4,739,901)</u>
Finance costs			
Distributions paid or payable		(2,282,738)	(2,226,151)
Decrease/(increase) in net assets attributable to unitholders		7,390,276	6,966,052
Net Profit		<u><u>-</u></u>	<u><u>-</u></u>
Basic earnings per unit (cents per unit)		<u><u>(157)</u></u>	<u><u>(148)</u></u>
Diluted earnings per unit (cents per unit)		<u><u>(157)</u></u>	<u><u>(148)</u></u>

The Income statement should be read in conjunction with the accompanying notes.

AUSTRALIAN ENHANCED INCOME FUND
ARSN 115 632 990
BALANCE SHEET
FOR THE YEAR ENDED 30 June 2009

	Notes	June 2008 \$	June 2008 \$
Assets			
Cash and cash equivalents	4	1,632,787	74,171
Trade and other receivables		205,993	611,122
Financial assets held at fair value through profit and loss	5	\$16,544,068	29,293,913
		<hr/>	<hr/>
Total Assets		18,382,848	27,979,206
Liabilities			
Trade and other payables		122,672	517,510
Financial liabilities	6	-	4,642,255
Distributions payable		569,893	552,663
		<hr/>	<hr/>
Total Liabilities (excluding net assets attributable to unitholders)		692,565	5,712,428
		<hr/>	<hr/>
Net assets attributable to unitholders	3	17,690,283	24,266,778
		<hr/>	<hr/>
Total Liabilities		18,382,848	27,979,206

The Balance Sheet statement should be read in conjunction with the accompanying notes.

AUSTRALIAN ENHANCED INCOME FUND
ARSN 115 632 990
CASHFLOW STATEMENT
FOR THE YEAR ENDED 30 June 2009

	Notes	June 2009 \$	June 2008 \$
Cashflows from Operating Activities			
Proceeds from the sale of securities		11,204,093	22,129,814
Purchases of securities		(5,397,563)	(26,287,902)
Dividends and distributions received		702,714	747,075
Interest received		1,472,634	1,951,399
Other income		2,500	-
Payments to suppliers		(262,862)	(395,675)
Interest paid		(49,396)	(156,793)
Net cash provided/(used) in operating activities		<u>7,672,120</u>	<u>(2,012,082)</u>
Cashflow from Financing Activities			
Proceeds from applications by unitholders		1,017,284	3,689,811
Units redeemed		(203,502)	(1,172,509)
Equity raising costs paid		-	-
Distributions paid		(2,282,738)	(2,314,833)
Net cash provided/(used) by financing activities		<u>(1,468,956)</u>	<u>202,469</u>
Net increase/(decrease) in cash		6,203,164	(1,809,613)
Cash at beginning of period		(4,568,084)	(2,758,471)
Cash at end of period		<u>1,632,786</u>	<u>(4,568,084)</u>

The Cashflow statement should be read in conjunction with the accompanying notes.

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AUSTRALIAN ENHANCED INCOME FUND
ARSN 115 632 990
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 30 June 2009

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 30 June 2009

1. STATEMENT OF SIGNIFICANT ACCOUNTING POLICIES

The financial report is a general purpose financial report that has been prepared in accordance with ASX Listing Rules.

The following is a summary of the material accounting policies adopted in the preparation of the financial report. The accounting policies have been consistently applied, and except where there is a change in accounting policy, are consistent with those of the previous year.

Basis of Preparation

The Company has prepared these financial statements in accordance with ASX Listing Rules. The financial statements have been prepared on an accruals basis and are based on historical costs with the exception of "held-for-trading" financial assets and certain other financial assets and liabilities which have been measured at fair value.

Accounting Policies

(a) Investments

i) Classification

Investments consist of listed securities and unlisted fixed interest securities.

It is considered that the information needs of shareholders in a company of this type are better met by stating investments at fair value rather than historical cost and by presenting the Balance Sheet on a liquidity basis.

ii) Valuation

All investments are classified as "held-for-trading" investments and are recognised at fair value, being the market value. Subsequent to the initial recognition, the changes in fair value are recognized in the income statement.

iii) Unrealised Gains and Losses

Unrealised gains and losses are included in operating profit for the year.

iv) Investment income

Dividend income is recognised in the Income Statement on the day on which the relevant investment is first quoted on an "ex-dividend" basis.

Interest revenue is recognised as it accrues, taking into account the effective yield on the financial asset.

v) Expenses

All expenses, including management fees and fund expenses are recognized in the income statement on an accruals basis.

b) Income tax

Under current legislation, the Fund is not subject to income tax provided the taxable income of the Fund is fully distributed either by the way of cash or reinvestment (i.e. the unitholders are presently entitled to the income of the Fund)

Financial instruments held at fair value may include unrealized capital gains. Should such a gain be realized, that portion of the gain that is subject to capital gains tax will be distributed so that the Fund is not subject to capital gains tax.

AUSTRALIAN ENHANCED INCOME FUND
ARSN 115 632 990
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 30 June 2009

1. STATEMENT OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Realised capital losses are not distributed to unit holders but are retained in the Fund to be offset against any realized capital gains. If realized capital gains exceed realized capital losses, the excess is distributed to unit holders.

The benefits of imputation credits and foreign tax paid are passed onto unitholders.

The Fund may incur withholding tax imposed by certain countries on investment income. Such income is recorded net of the withholding tax in the income statement.

c) Distributions

In accordance with the Fund Constitution, the Fund fully distributes its distributable (taxable) income to unit holders by cash or reinvestment. The distributions are recognized in the income statement as finance costs attributable to unit holders.

(d) Cash and Cash Equivalents

Cash and cash equivalents include cash on hand, at call deposits with banks or financial institutions.

(e) Trade and Other Receivables

Trade and other receivables are stated at their amortised cost less impairment losses (refer Note 1(g)).

(f) Trade and Other Payables

Trade and other payables are stated at their amortised cost.

(g) Impairment of Assets

At each reporting date, the Company reviews the carrying values of its tangible assets to determine whether there is any indication that those assets have been impaired. If such an indication exists, the recoverable amount of the asset, being the higher of the asset's fair value less costs to sell and value in use, is compared to the asset's carrying value. Any excess of the asset's carrying value over its recoverable amount is expensed to the Income Statement.

(h) Goods and Services Tax

Revenues, expenses and assets are recognised net of the amount of goods and services tax (GST), except where the amount of the GST incurred is not recoverable from the Australian Taxation Office (ATO). In these circumstances the GST is recognised as part of the cost of acquisition of the asset or as part of an item of the expense.

Receivables and payables are stated inclusive of GST. The net amount of GST recoverable from, or payable to, the ATO is included as an asset or liability in the Balance Sheet.

Cash flows are presented in the Cash Flow Statement on a gross basis, except for the GST component of investing and financing activities, which are disclosed as operating cash flows.

(h) Segment Reporting

The Company is engaged in investment activities conducted in Australia and derives revenue and investment income from listed, unlisted and fixed interest securities.

AUSTRALIAN ENHANCED INCOME FUND
ARSN 115 632 990
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 30 June 2009

2. REVENUE FROM ORDINARY ACTIVITIES

(a) Revenue	June 2009 (\$)	June 2008 (\$)
Dividends & distributions	686,242	740,075
Interest	1,416,422	1,942,078
Realised gain/(loss)	(373,049)	(847,626)
Other Income	2,500	7,000
Total Revenue	(4,768,828)	(4,221,102)
(b) Net gain/(loss) on financial assets held at fair value through profit and loss	June 2009 (\$)	June 2008 (\$)
Unrealised gain/(loss) on investments	(6,501,313)	(6,063,260)
Total gain/loss	(4,768,828)	(4,221,102)

3. NET ASSETS ATTRIBUTABLE TO UNITHOLDERS

Movements in the number of units and net assets attributable to unitholders during the period were as follows.

	June 2009 No.	June 2009 (\$)
Opening balance	3,158,070	24,266,778
Applications	133,458	1,017,284
Redemptions	(35,000)	(203,503)
Profit attributable to unitholders before income tax		(5,107,269)
Distributions paid or payable		(2,282,738)
Closing balance	3,256,528	17,690,552

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NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 30 June 2009

3. NET ASSETS ATTRIBUTABLE TO UNITHOLDERS (CONTINUED)

	June 2008 No.	June 2008 (\$)
Opening balance	2,915,222	28,715,528
Applications	384,348	3,689,813
Redemptions	(141,500)	(1,172,509)
Profit attributable to unitholders before income tax		(4,739,901)
Distributions paid or payable		(2,226,151)
Closing balance	3,158,070	24,266,778

The following rights and benefits are attached to the units on issue.

As stipulated in the Fund Constitution, each unit represents a right to an individual share in the Fund and does not extend to a right to the underlying assets of the Fund. There are no separate classes of the units and each unit has the same rights attaching to it as all other units of the Fund.

Voting

Voting is by a show of hands unless a poll is demanded. The Corporations Act 2001 governs who can demand a poll and the value of each vote required to pass a resolution. The Chair of the meeting has no casting vote.

Distributions

The Fund intends to distribute all of its taxable profits each year to unitholders.

Redemptions

The manager offers a facility for the redemption of units on 4 dates during the year. Units can only be redeemed at the exit price.

Winding up

After paying or making allowance for anticipated liabilities, subject to the rights and obligations attaching to any class, the net proceeds must be distributed pro-rate to investors according to the number of units they hold at termination.

4. CASH AND CASH EQUIVALENTS

Cash as at the end of the financial year is as follows:

	June 2009 (\$)	June 2008 (\$)
Cash at bank	<u>1,632,787</u>	<u>74,171</u>

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AUSTRALIAN ENHANCED INCOME FUND
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NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 30 June 2009

5. FINANCIAL ASSETS HELD AT FAIR VALUE THROUGH PROFIT AND LOSS

	June 2009 (\$)	June 2008 (\$)
Listed investments	16,544,338	29,293,193
	<u>16,544,338</u>	<u>29,293,193</u>

6. FINANCIAL LIABILITIES

	June 2009 (\$)	June 2008 (\$)
Borrowings	<u>-</u>	<u>4,642,2551</u>

7. SEGMENT INFORMATION

The Australian Enhanced Income Fund is a registered managed investment scheme, incorporated and domiciled in Australia. The Fund's principal activity is investment management, conducted primarily in Australia.