



Fund Update

“Australian Leaders is offering investors an alternative to a traditional equity fund, most of which have performed poorly since the advent of the financial crisis. Over the last 5 years ALF has grown by 60% while the market and most institutional funds have moved sideways”.

Justin Braitling
Chairman



Australian Leaders Fund Limited (ALF)

Australian Leaders is a listed investment company that invests in the shares of leading and emerging companies listed on the Australian Stock Exchange. ALF is different to a traditional fund in its use of hedging strategies to enhance returns and manage risk.

DIRECTORS:

J. BRAITLING (CHAIRMAN)
G. WILSON
J. ABERNETHY
J. GOSSE

Shares Outstanding: 69 million
Market Capitalisation @ \$1.14: \$79 million
NTA @ April 2012 \$1.26 after tax
Discount- 10%

Watermark Funds Management

We are active, high conviction investors in Australian public companies. As an Absolute Return manager, Watermark offers a proven alternative to traditional institutional funds.

Established in 2004 by Justin Braitling, who has over 20 years experience managing portfolios of Australian and International shares, Watermark comprises a team of dedicated and experienced investment professionals based in Sydney.

Chief Investment Officer
Senior Analyst
Industrial Analyst
Operations Manager

Justin Braitling
Tom Richardson
Joshua Ross
Nerida Dawson

Benefits of a Listed Investment Company

ALF has some important advantages over unlisted funds:

- As a listed company ALF can retain and accumulate earnings in a tax effective manner offering greater control over the distribution of returns to investors.
- Since listing back in 2004, the company has paid consistent and progressive dividends to shareholders including special dividends in years when the fund has performed well.
- The board is committed to active capital management having successfully completed a number of share buy backs at times when the shares have been undervalued by the market.



About ALF

Our investment process is similar to other funds with a primary goal of identifying mispriced shares. We look to buy good companies on occasions when they are undervalued by the market.

However, ALF is different to a traditional fund in moving to the next logical step and also selling (short) the shares of businesses that are fundamentally challenged.

As shorts are a natural hedge for the company's assets if shares fall in value, we are better equipped to manage risk through the cycle.

Investment Philosophy

The best investment opportunities are found in well managed companies with strong business fundamentals that can be purchased on attractive terms.

These companies typically exhibit the following characteristics:

- A history of superior returns through the economic cycle
- Management with a track record of creating and distributing value to shareholders
- Businesses with a capacity to grow

Consistent with these basic principles, in selecting shares to **short sell**, the Manager looks for companies with **weak fundamentals** that can be sold for more than they are worth.



Investment Objective

Profit from the mispricing of Australian shares while protecting our investors from loss

Since listing 8 years ago, ALF has exceeded all targets.

Strong Stock Selection

	TARGET	5yr Performance
Long Portfolio	+ 3-5% Outperformance	+8%
Short Portfolio	- 3-5% Under-performance	-5%

Protected our shareholders from loss

In 2009 when the market fell by 22%, ALF increased by 19%, net of all fees.

Security selection has been a strength



We picked the best industrial shares in recent years

FY 2009

- 1. RHG Group -Rams Home
- 2. Decmil
- 3. Customers
- 4. FlexiGroup
- 5. Cash Converters

Started Buying: Nov 2008 @ 12c
Sold into Buy Back at 64c



ALF becomes substantial shareholder in Feb-2009

Featured in *Leading Edge* May 2009

FY 2011

- 1. Mesoblast
- 2. Ainsworth Gaming
- 3. Imdex
- 4. NRW Holdings
- 5. Starpharma Holdings

Started Buying: Feb 2009 @ 78c
Sold between \$8-\$9



First featured in *Leading Edge* -Dec'09

FY 2012 YTD

- 1. Ainsworth Gaming
- 2. Customers
- 3. Domino Pizza
- 4. A.P. Eagers
- 5. Amcom Telco

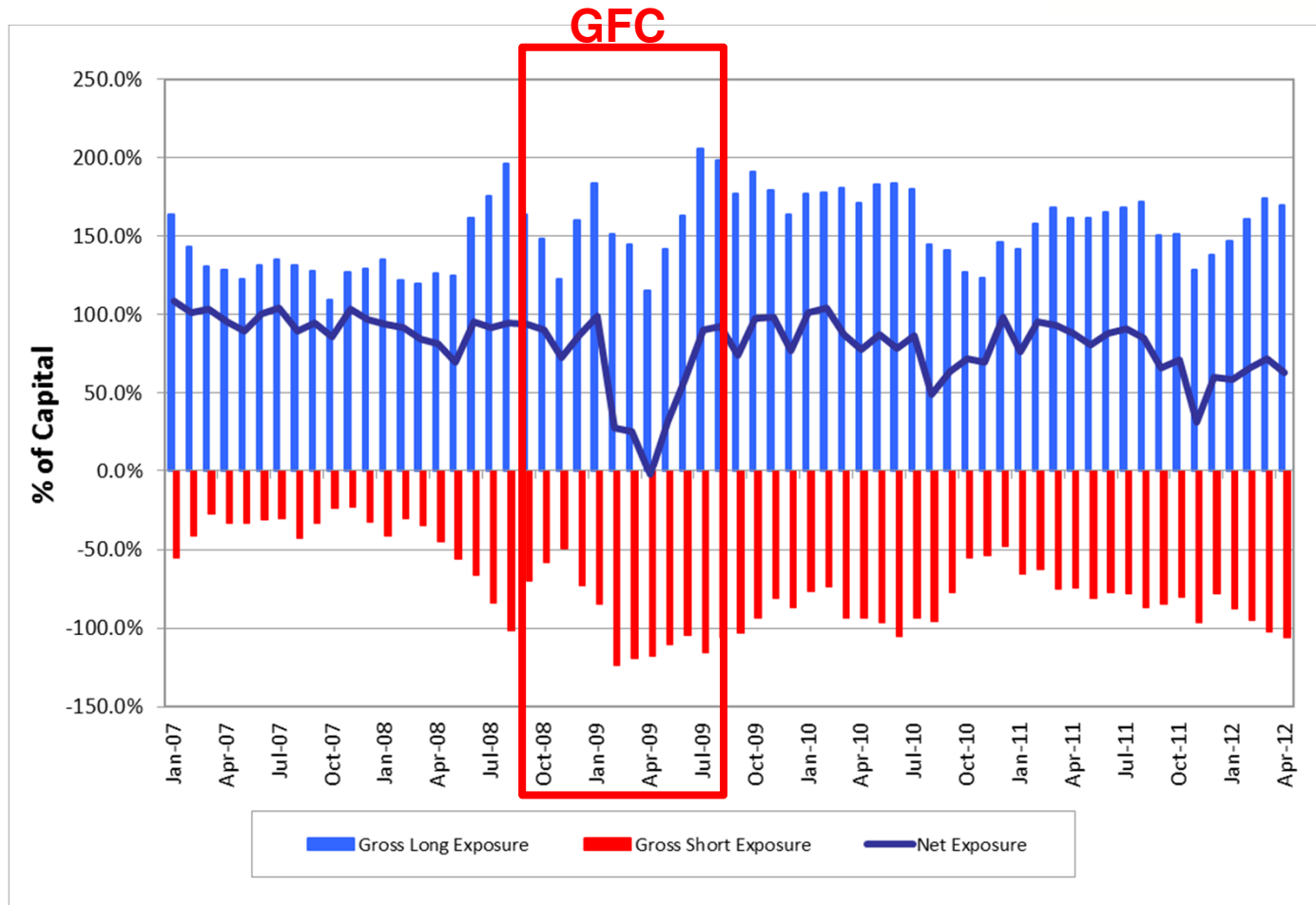
Started Buying: June 2011 @ 38c. Still see lots of upside at \$1.80.



Only institutional shareholder on register, just below substantial when featured in *Leading Edge* -Dec 2011

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We have protected your capital



In the 2009 financial year ALF's shareholder funds increased 26% while the All Ordinaries Index fell by 22%.

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How we pick shares to buy and sell (short)



Fundamental Analysis: Shares move up or down over time as value is created or lost in a business. We focus on the following key value drivers:

Long/Short Example

Industry Structure



Barriers to entry
Growth
Structural Change

Seek Vs Fairfax Newspapers

Business Fundamentals



Porter Analysis

Coca-Cola Vs Goodman Fielder

Management



Strategy
Operation Strength
Capital Management

NAB Vs ComBank

Industry Structure

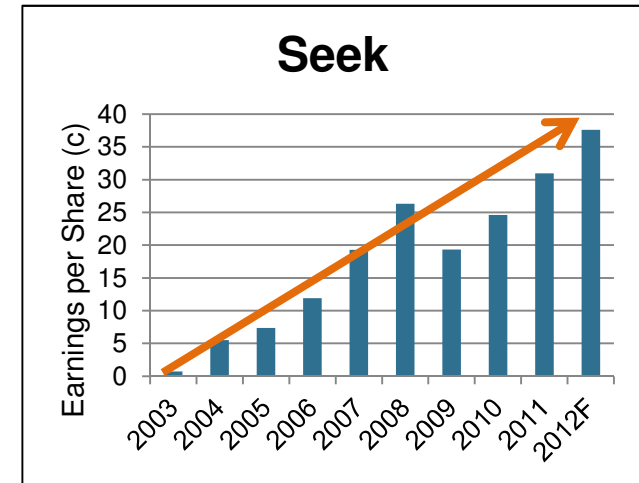


“New entrants can leapfrog the industry leaders and alight on the new experience curve, to which the leaders may be poorly positioned to jump” – Michael Porter, Competitive Strategy 1980.

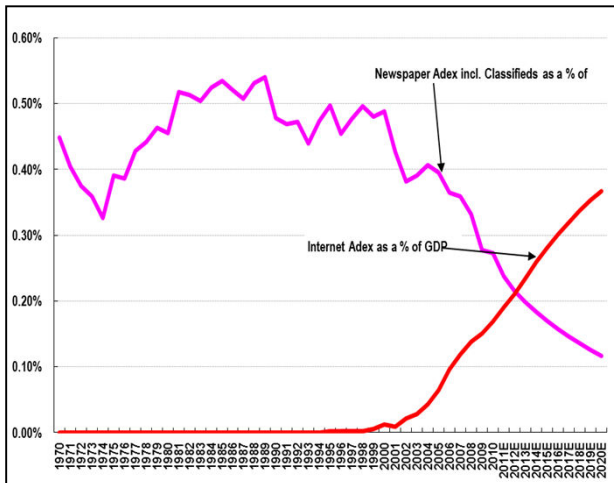


BUY – Seek

- Disruptive technology championed by entrepreneurial brothers.
- Consumer demands for online product has driven revenues from old media to new media.
- Highly scalable model has translated into strong financial performance.

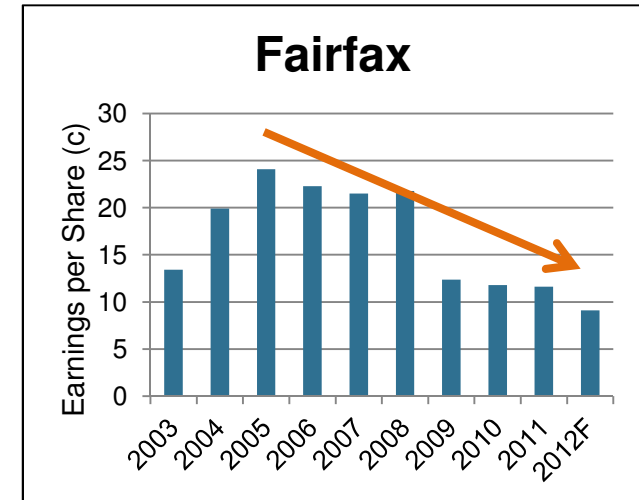


Changing Composition of Advertising as a % of GDP



SELL – Fairfax

- Management revolving door as industry fundamentals destroy the reputation of numerous CEOs.
- Encumbered balance sheet restricted the ability to quickly transition the business.
- Legacy cost base and revenue leakage to new entrants has significantly impacted financial returns.

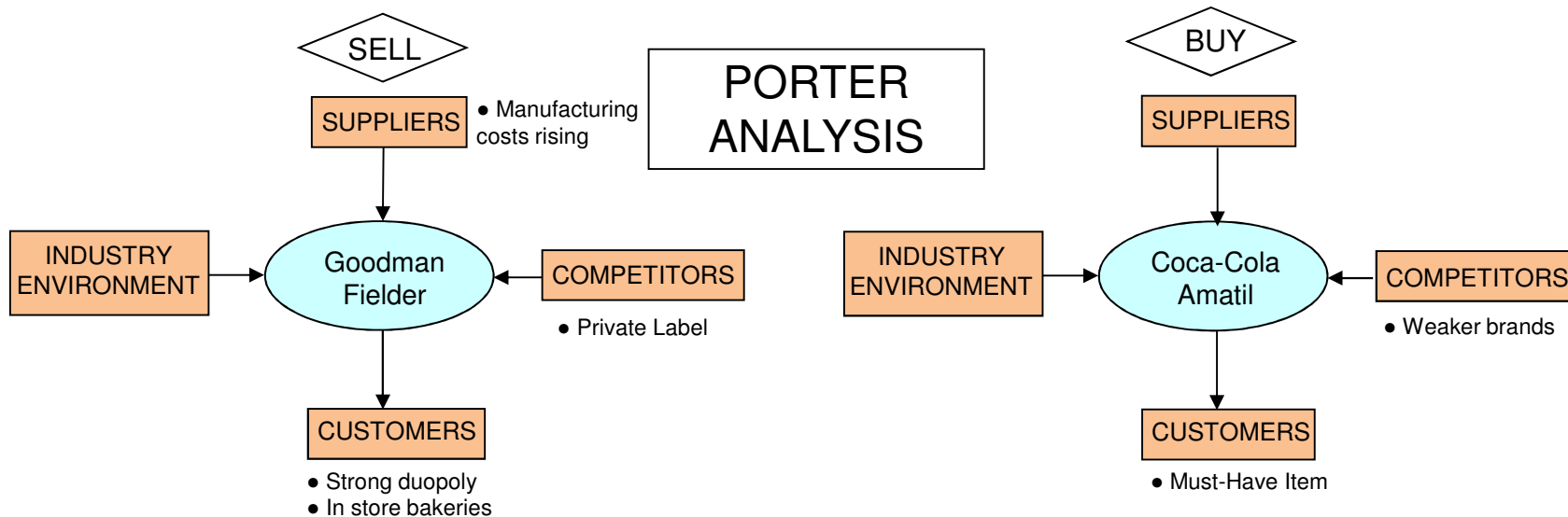
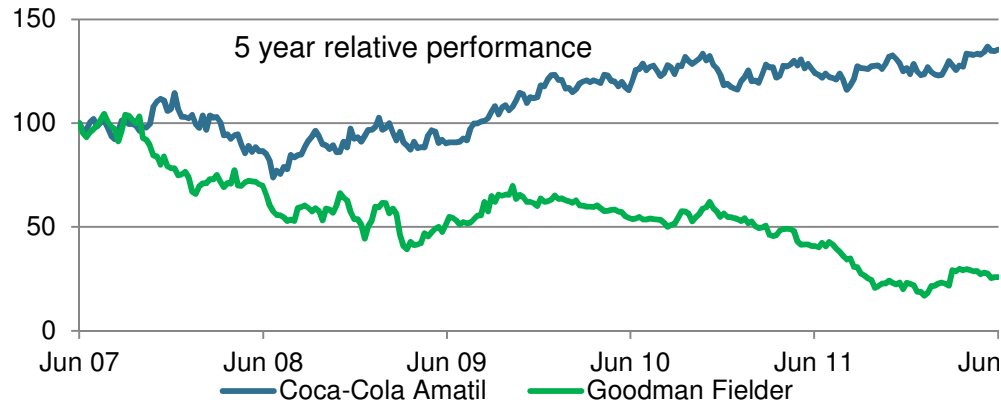


Source: Morgan Stanley Research Estimates

Business Fundamentals



Both GFF and Coke are well known branded food groups. While Coke dominates the CSD category and has improved terms with retailers, Goodman has been decimated by higher commodity prices, substitution and deteriorating trading terms.

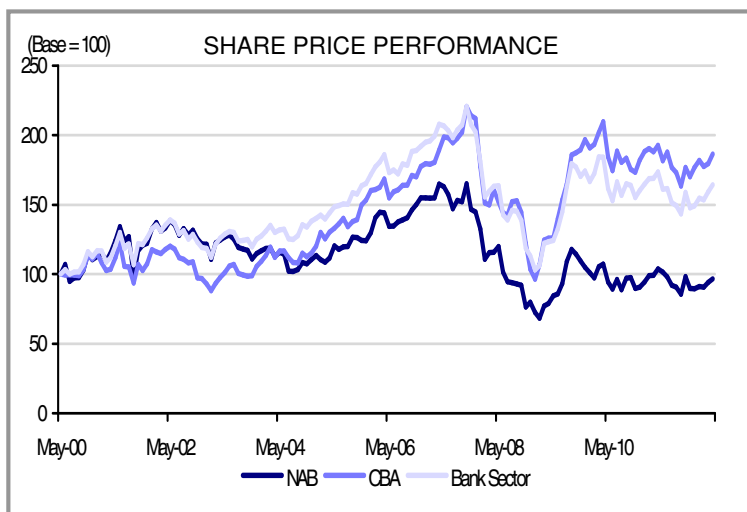


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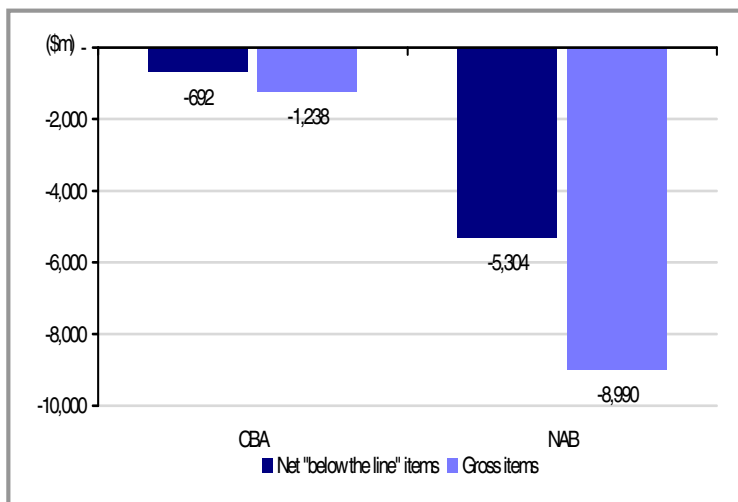
Management



Over 12 years NAB shares are unchanged while Commbank shares doubled in value



'BELOW THE LINE' ADJUSTMENTS



A long series of failures:

Poor Earnings quality

A \$5.3bn divergence between Cash profit and a more conservative measure with 47 "below the line" items over 12 years

Terrible capital management - Acquisitions

- NAB overpaid for MLC - 2000
- Homeside impairment
- NAB acquires stake in AMP Sep-2003
- Great Western Bank acquisition Nov-2007
- Failed AXA acquisition attempt Dec-2009

Poor operational controls

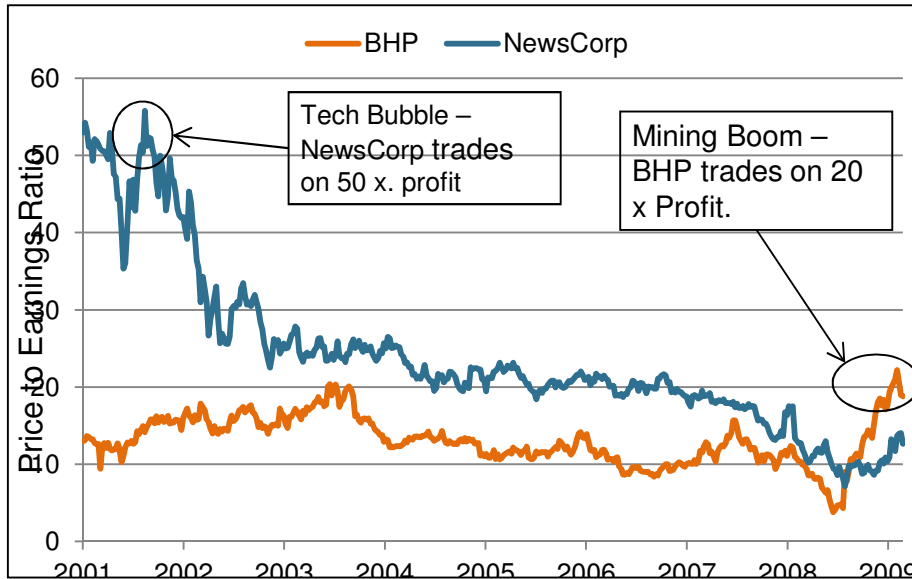
- FX trading losses Jan-2004
- Material profit warning after capital raising Jul-2004
- CDO losses Jul-2008

Strategy and execution

Personal Bank strategy for NAB has grown the business unprofitably while vs ComBank has successfully grown its Business Bank

Valuation

Tech Bubble to Mining Boom



Shares can also move away from fundamental value providing opportunities to Buy and Sell

During the tech bubble, NewsCorp was highly rated with the expectation that profits would expand with the adoption of new technologies.

At the same time, old world industries were shunned by investors with many companies starved of capital. Investment in mine production collapsed

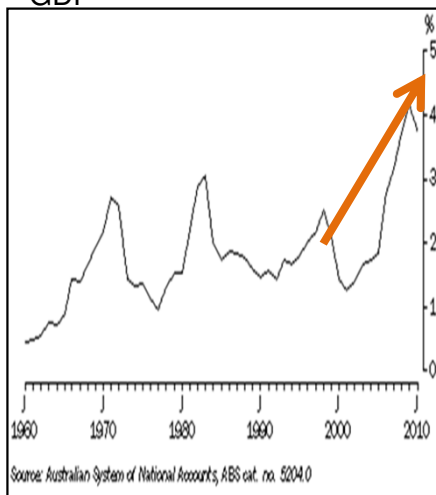
Investors flocked to the TMT sector pushing up sector valuations, leaving mining shares looking cheap.

This resulted in a lack of resource development at a time when China was rapidly industrialising.

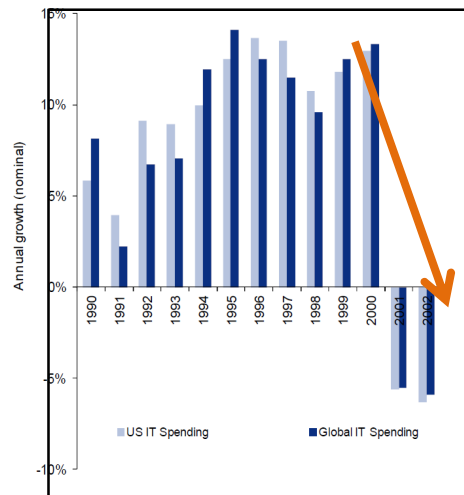
Ultimately manifesting in significantly higher commodity prices and generous returns for investors in mining.

By the time the boom was in full swing in 2009, BHP was more highly rated than many TMT companies with better structural growth.

Mining Investment: Share of GDP



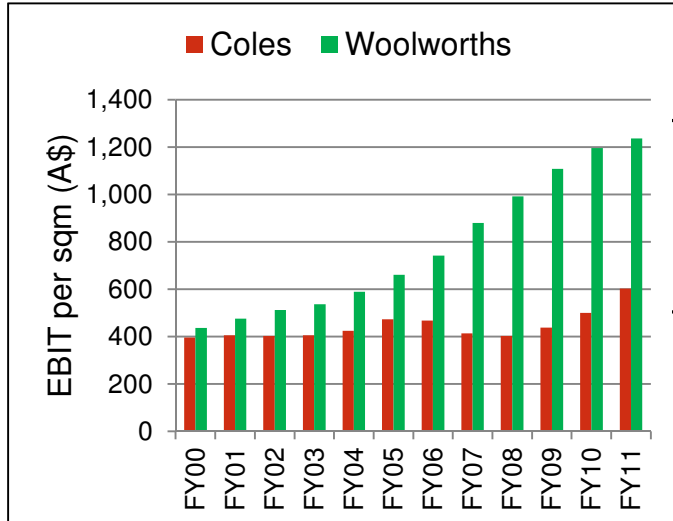
Global IT spending Growth



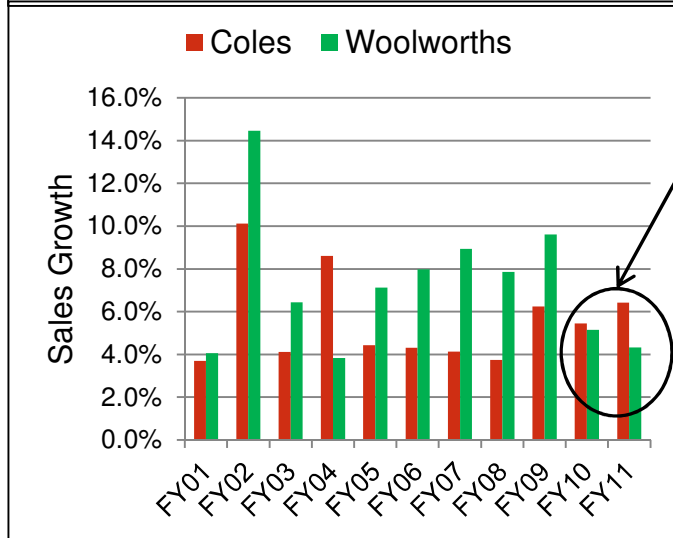
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Opportunity:

New management leading renewal at Coles



Significant potential to close profit gap



Coles is now out-trading Woolies

BUY - Wesfarmers

- Has successfully driven foot traffic and sales via execution of proven retail strategy:
 - Focus on Fresh
 - Price Leadership – especially on regular items
 - Increased service to customers
- Wesfarmers trades on the same multiple as Woolworths despite the clear opportunity to increase the profitability of the network.
- Wesfarmers has a portfolio of other strong business, led by market leader Bunnings.

SELL - Woolworths

- Unsettled by disruptive Coles marketing, and losing sales momentum.
- Has lost consumers perception of Price Leader.
- Is pushing suppliers hard on terms, with stores arguably operating at optimal efficiency.
- Investing significant capital in building Masters, diluting near-term returns to shareholders.

Opportunity: Emerging growth company

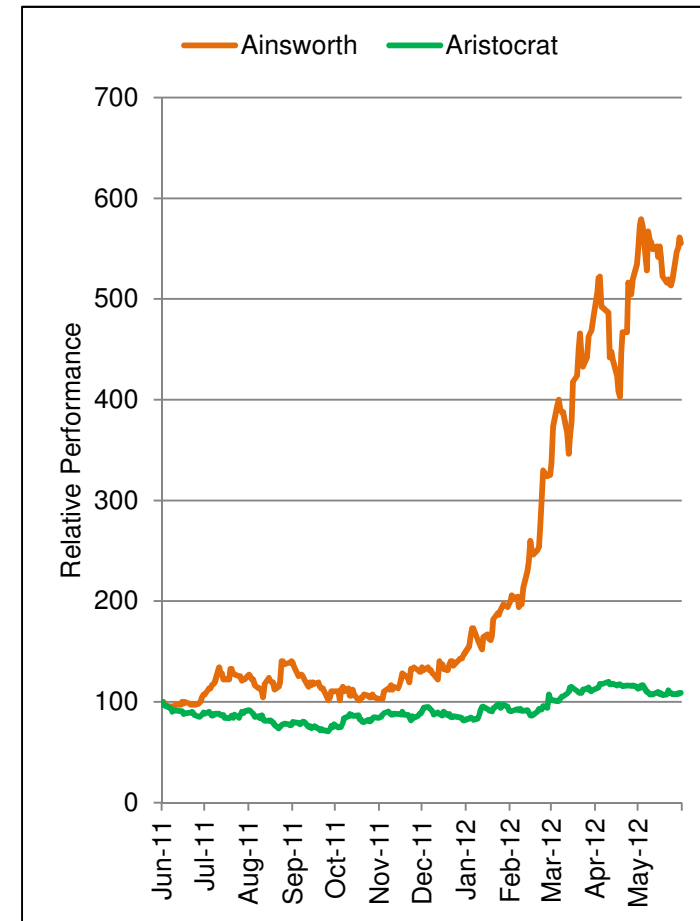


BUY – Ainsworth

- Visionary management team with impressive track record.
- Superior performing games is driving increased demand for Ainsworth product.
- Underperformance of Australian incumbent has presented the opportunity for Ainsworth to take market share.
- Massive market opportunity in the US despite the relatively small market capitalisation of the company.

SELL - Aristocrat

- New management from outside the industry without gaming experience
- Poor execution in rolling out new Meridian Cabinet provided Ainsworth with golden opportunity to take share
- Customers now talk about new and old games for ALL the problem is while the old games continue to do well like 'Queen of the Nile" the new games are struggling





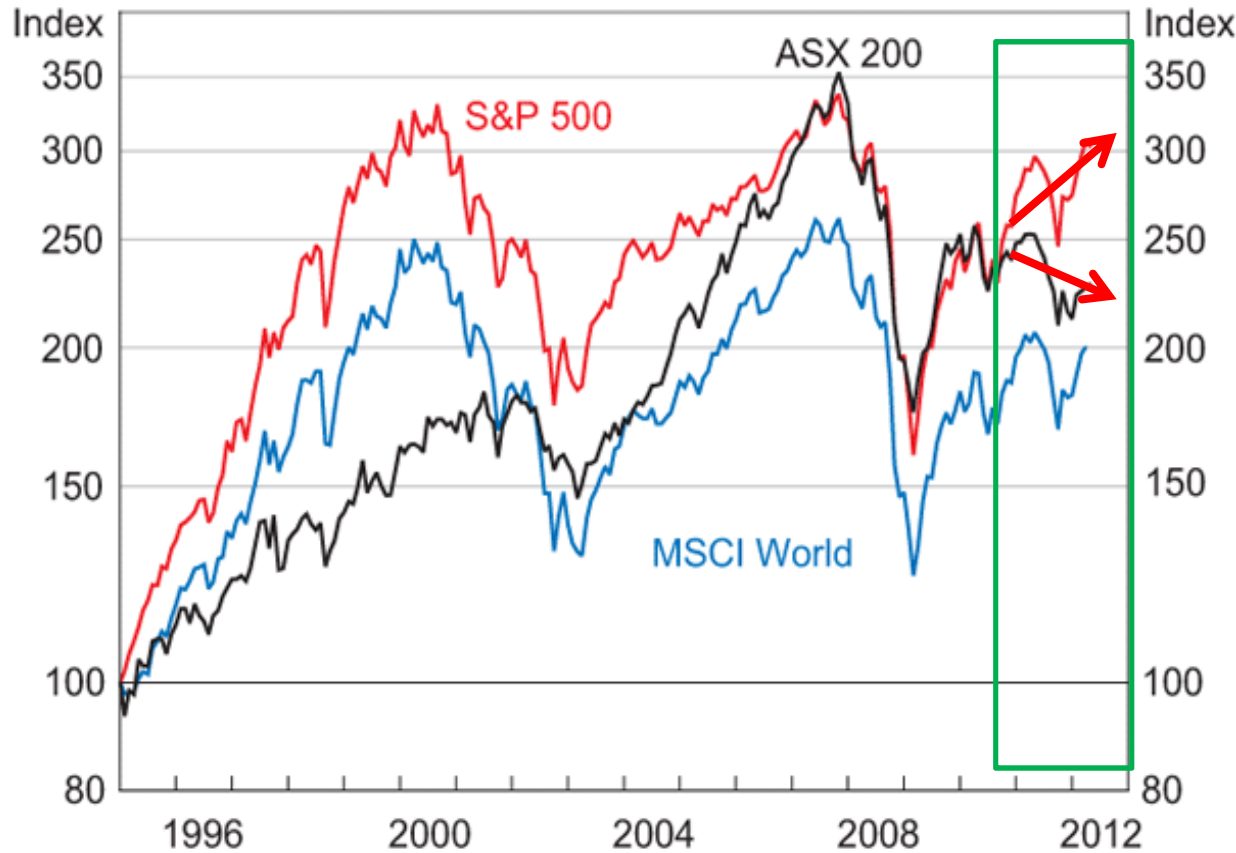
Industrial Companies under Pressure

Our market has underperformed



Australian and World Share Price Indices

Log scale, end December 1994 = 100



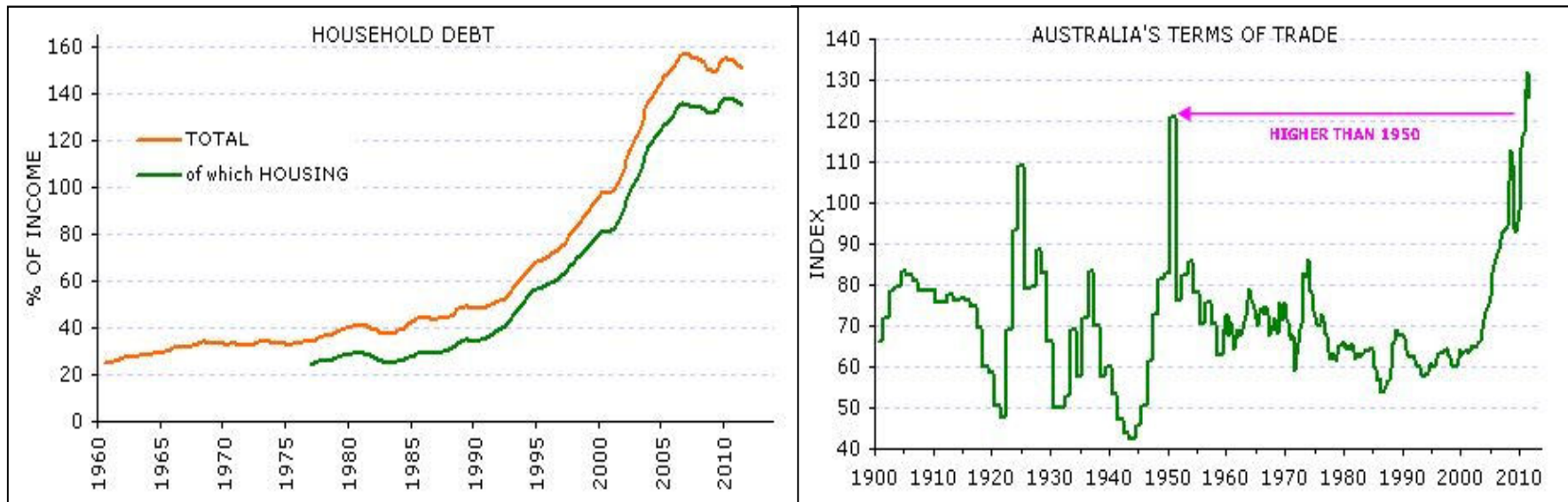
Sources: Bloomberg; RBA; Thomson Reuters

- Australian industry, outside mining, is struggling.
- US corporate profits are recovering from a deep recession
- Mining shares have fallen as China slows

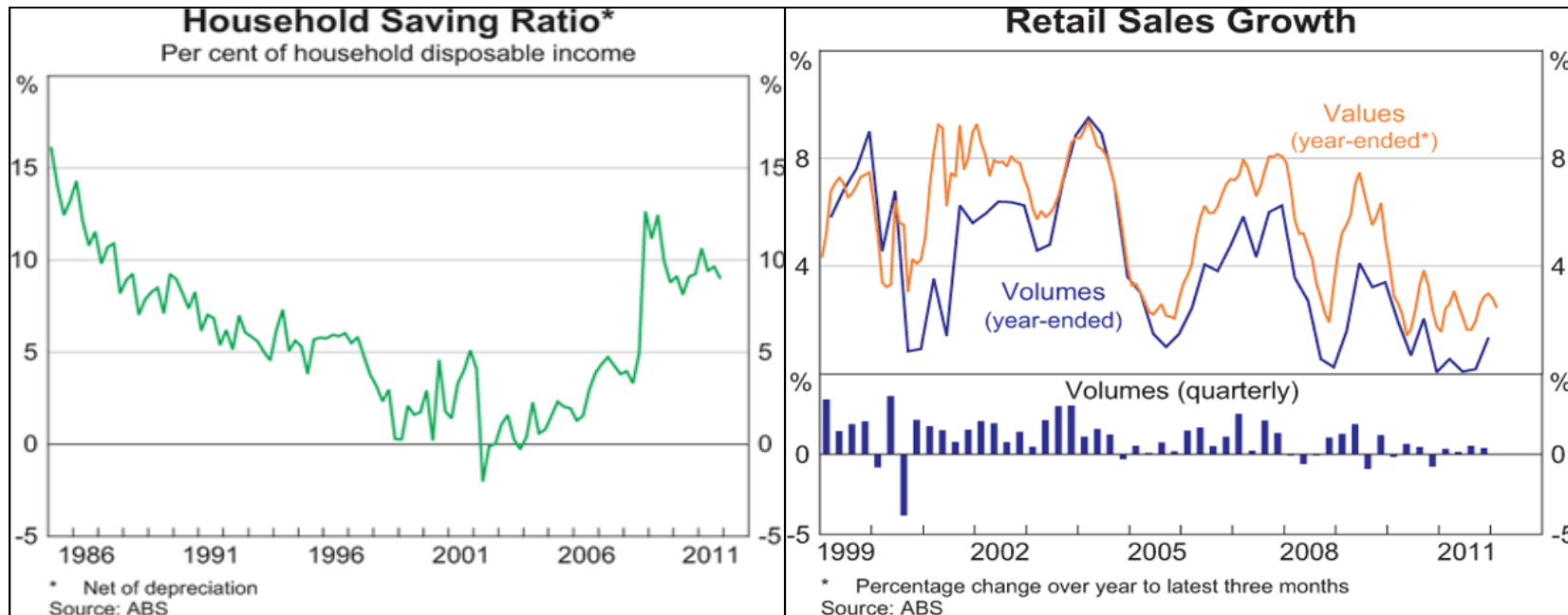
Two significant tailwinds now reversing



20 Years of Household Leverage & Terms of Trade Peaking

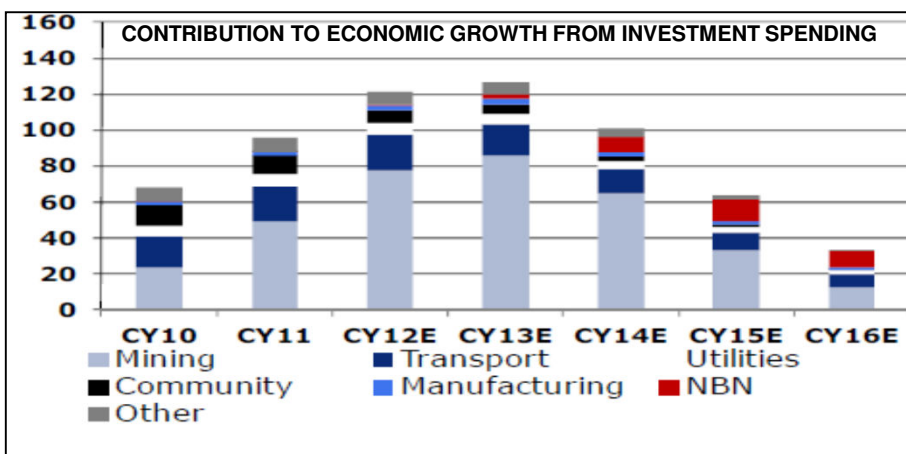


Households and businesses are now retrenching

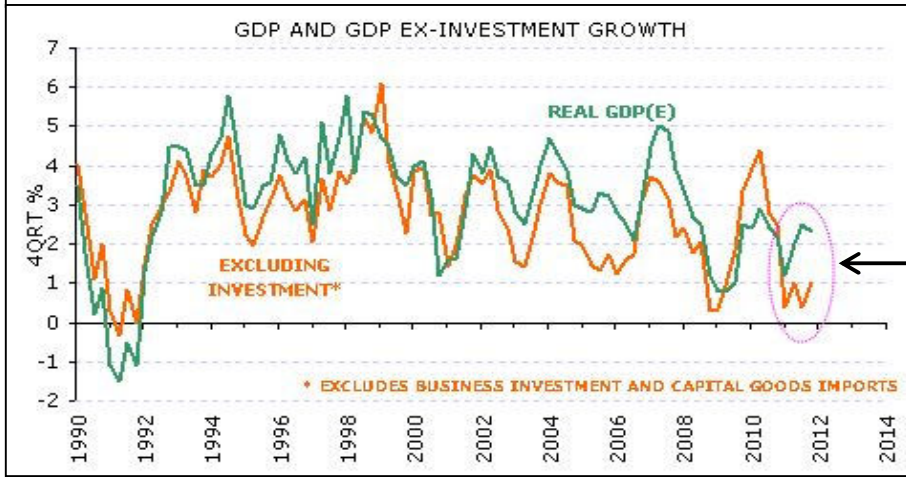


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The economic benefit from mining investment is peaking now also



Source: Goldman Sachs Global ECS Research, Deloitte Access Economics.



Mining accounts for half of all sanctioned investment projects.

Global mining companies are thinking twice about investing in Australia

- High capital costs – RIO Mount Pleasant
- Divisive unions – BMA Coal mines
- Offshore labour (EMAs) – Hancock Iron Ore
- Land-owner rights – Santos GLNG
- High level of compliance – BG QCLNG
- Infrastructure costs – Xstrata Wandoan
- Operating costs – BMA Norwich Park

Clear evidence of the two-speed economy

Australian businesses are struggling

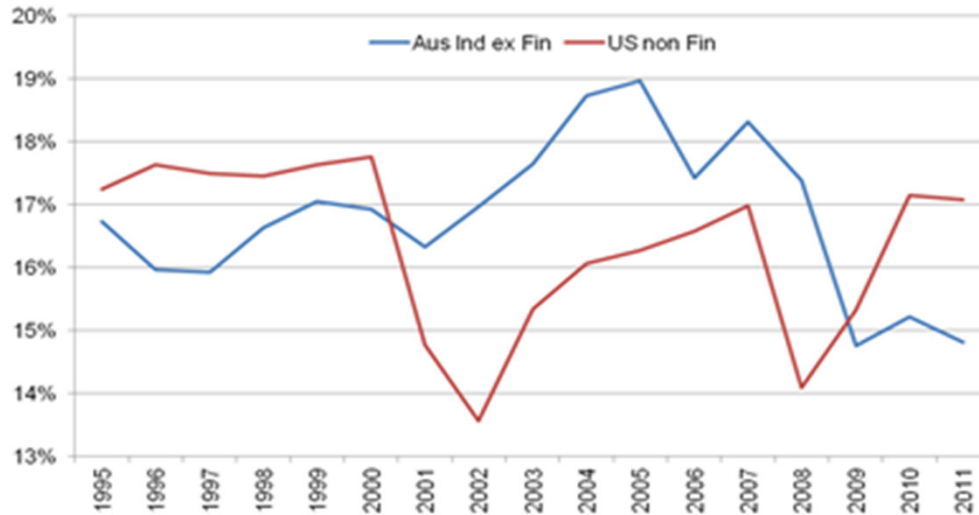


SECTOR WEIGHT AND PROFIT GROWTH AUSTRALIA Vs U.S.

Sector	Index weight		Profit growth (2012)	
	S&P 500	ASX 200	S&P 500	ASX 200
Energy & materials	14%	29%	0%	3%
Industrials	12%	8%	9%	-3%
Consumer goods & services	23%	13%	6%	-3%
Healthcare	11%	4%	0%	-1%
Telecoms & utilities	6%	7%	-2%	0%
Financials	16%	40%	22%	0%
Technology	19%	0%	10%	-5%
Total	100%	100%	7%	0%

- Financial conditions are incredibly tight
 - High interest rates
 - Strong currency
- Poor productivity trends
- Businesses and consumers are deleveraging
- Housing Cycle rolling over
- Deflation endemic

INDUSTRIAL COMPANY PROFIT MARGINS AUS VS U.S.





Portfolio Construction and Performance

Fund Snapshot

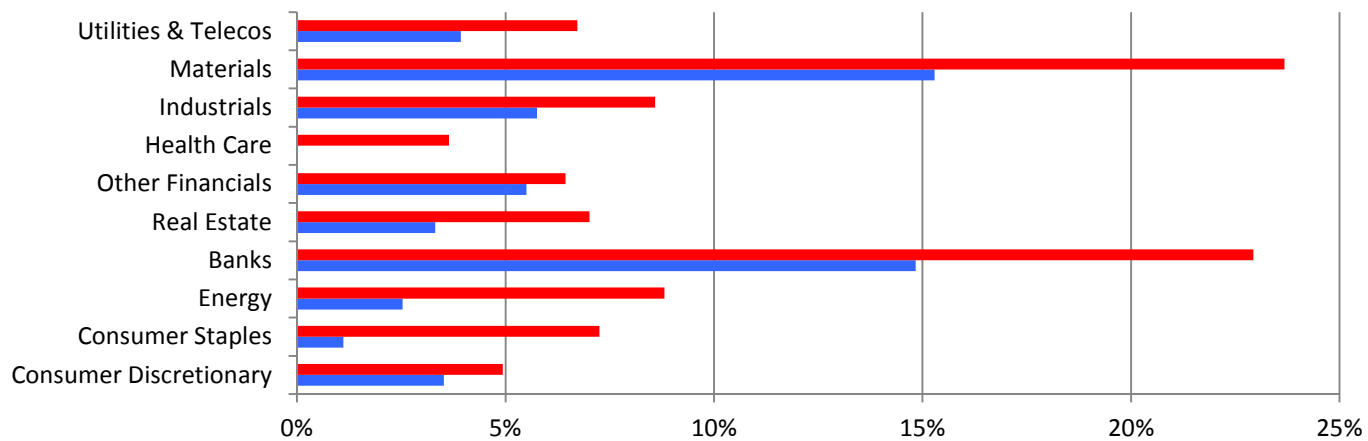
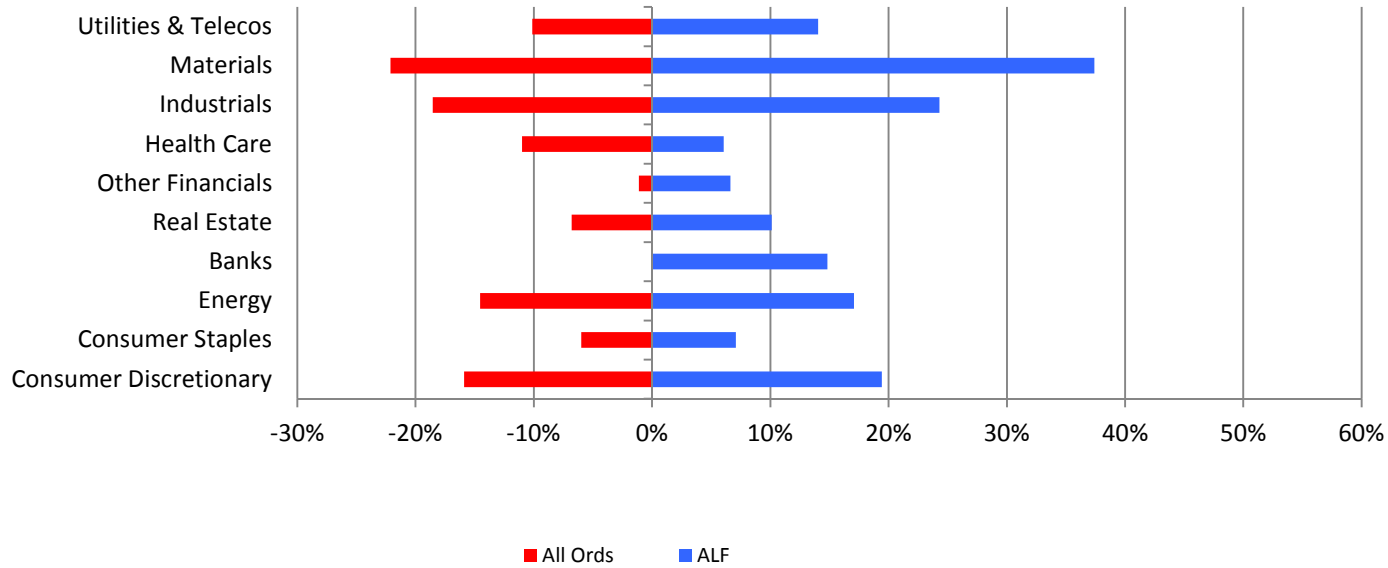
Fund Statistics	
Fund NAV AUD (Millions)	86.1M
Long (79)	157%
Short (58)	-106%
Gross Exposure	263%
Net Exposure	51%
Cash	49%

Top 10 Long Holdings	
BHP Billiton Ltd.	8.2%
Westpac Banking Corp.	6.2%
Wesfarmers Ltd.	6.0%
Telstra Corp. Ltd.	6.0%
Ainsworth Game Technology	5.1%
Orica Ltd.	4.5%
Origin Energy Ltd.	4.5%
Rio Tinto Ltd.	4.5%
Transurban Group	4.4%
DUET Group	3.6%

Top 10 Short Holdings	
Amcor Ltd.	-5.4%
Caltex Australia Ltd.	-4.1%
Iluka Resources Ltd.	-3.9%
Ansell Ltd.	-3.4%
Computershare Ltd.	-3.3%
Sydney Airport	-3.0%
Sigma Pharmaceuticals Ltd.	-3.0%
Wotif.com Holdings Ltd.	-2.8%
Medusa Mining Ltd.	-2.7%
AGL Energy Ltd.	-2.6%

All data as of 30 April 2012

Portfolio Exposure

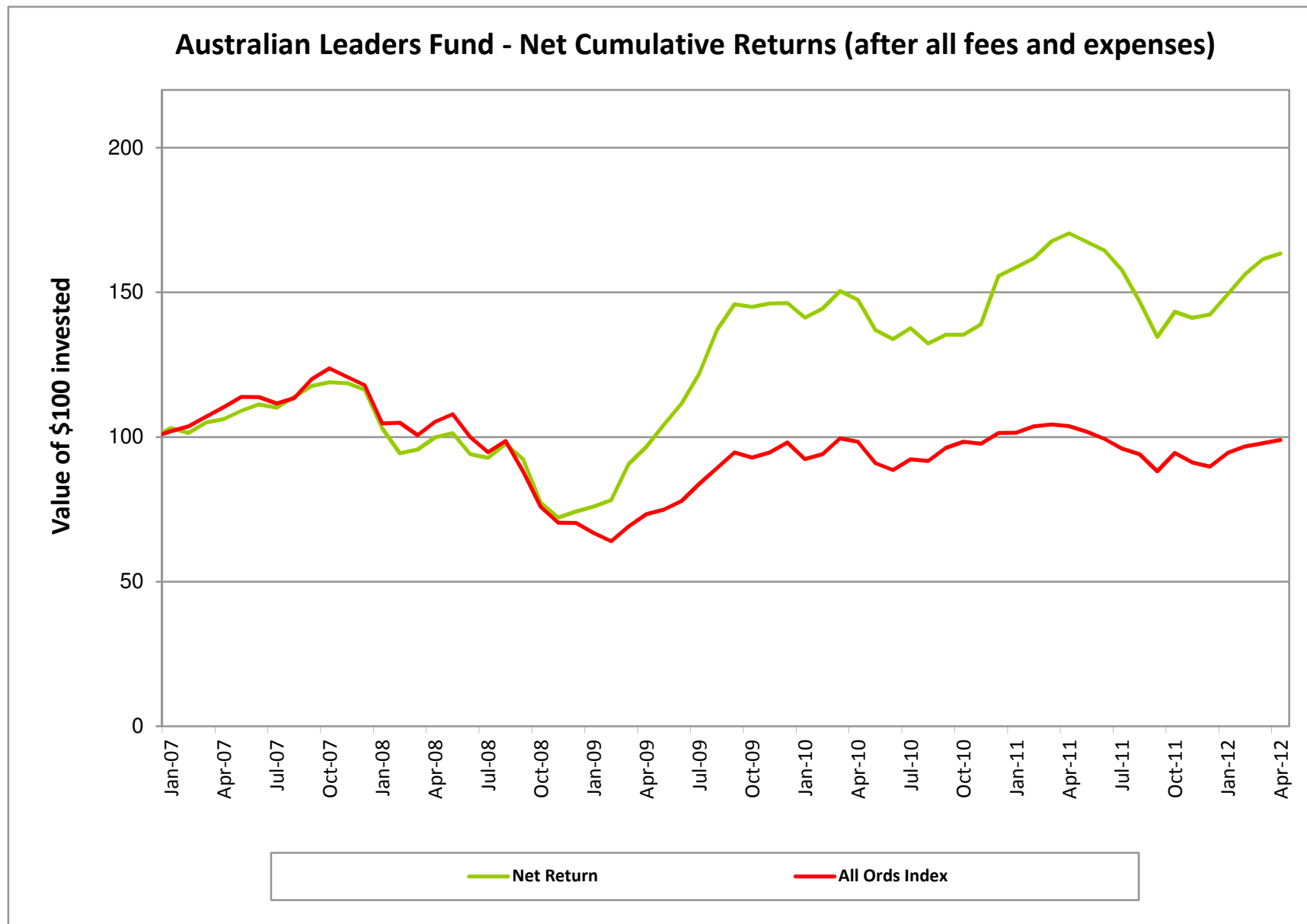


All data as of 30 April 2012

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Asset Allocation

SECTOR	LONG	SHORT	ALF NET	Market
Defensive	40%	28%	12%	20%
Financial	31%	12%	19%	35%
Industrial Cyclical	32%	34%	-2%	13%
Resources	40%	24%	16%	23%
Small Companies	7%	5%	2%	8%
Equity Exposure	150%	102%	48%	100%
Listed Bonds & Hybrids	14%		14%	



LICs Performance



	1 Year	3 Years pa	5 Years pa	7 Years pa	10 Years pa	15 Years pa	20 Years pa
Australian Foundation Investment Company Ltd	-3.4%	12.0%	0.3%	6.4%	8.0%	10.0%	11.0%
Aberdeen Leaders Limited *	-17.1%	5.9%	-6.6%	1.7%	3.4%	6.2%	-
AMCIL Limited	7.4%	19.0%	6.2%	10.9%	16.2%	12.9%	-
Argo Investments	-5.5%	11.3%	-1.8%	4.8%	7.2%	9.4%	10.6%
Australian Leaders Fund Limited *	-3.7%	15.5%	6.0%	10.2%	-	-	-
Australian United Limited *	-9.1%	11.4%	-2.1%	5.3%	7.5%	9.7%	-
Brickworks Investment Company *	0.3%	13.1%	1.0%	6.1%	-	-	-
Contango MicroCap Limited	-7.6%	18.1%	-1.4%	7.9%	-	-	-
Century Australian Investments Limited *	-9.9%	9.5%	-2.3%	3.1%	-	-	-
Djerriwarrh Investments Limited	-4.4%	11.0%	-1.2%	5.2%	6.4%	8.0%	9.2%
Diversified United Investments Limited *	-9.1%	9.8%	-2.5%	5.4%	7.4%	9.3%	9.6%
Emerging Leaders Investments Limited	-8.9%	15.8%	-1.3%	4.3%	-	-	-
Ironbark Capital Limited *	3.2%	12.3%	1.1%	3.8%	4.0%	5.0%	6.5%
Mirrabooka Investments Limited	7.1%	20.5%	2.0%	7.7%	10.7%	-	-
Milton Corporation *	-0.7%	12.4%	-0.7%	5.4%	7.6%	10.9%	-
Spider S&P/ASX 50 Fund	-5.6%	10.4%	-1.5%	5.3%	6.4%	-	-
Spider S&P/ASX 200 Property Fund	-1.9%	12.6%	-13.6%	-4.9%	0.8%	-	-
Spider S&P/ASX 200 Fund	-6.4%	10.8%	-2.3%	4.9%	6.6%	-	-
WAM Capital Limited *	-0.8%	14.5%	1.5%	6.5%	8.0%	-	-
Whitefield Limited *	-4.5%	9.0%	-6.4%	0.5%	-	-	-
WAM Research Limited*	-3.0%	7.5%	-4.8%	1.1%	-	-	-
S&P/ASX All Ordinaries Accumulation Index	-6.2%	12.3%	-1.8%	5.4%	7.1%	8.4%	9.3%
S&P/ASX 50 Leaders Accumulation Index	-7.1%	10.1%	-1.6%	5.3%	6.5%	8.6%	9.9%

Source: JBWere Listed Investment Companies, April 2012

Portfolio Returns



ALF	6 MONTHS	FYTD	1 YEAR	3 YEARS (P.A.)	5 YEARS (P.A.)	SI (P.A.)
Long	12.3%	2.3%	-2.2%	22.5%	8.0%	-
Short	4.0%	1.3%	-4.2%	10.9%	-4.7%	-
Gross	15.6%	1.5%	-1.5%	24.5%	13.2%	17.4%
Net	14.1%	-0.7%	-4.1%	19.1%	9.0%	13.9%
Index	4.7%	-0.4%	-4.6%	10.5%	-2.2%	8.2%

Performance to 30 April 2012