Quarterly Outlook Presentation

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Global Economic Perspective

	Year		
	2007	2008	2009
Real GDP Growth			
United States	2.2	1.4	1.3
Germany	2.5	1.7	1.6
Japan	2.0	1.3	1.6
Australia	3.9	3.2	3.3
Consumer Price Inflation			
United States	2.9	4.8	2.3
Germany	2.3	2.5	1.9
Japan	0.0	0.8	0.5
Australia	3.0	4.1	3.5

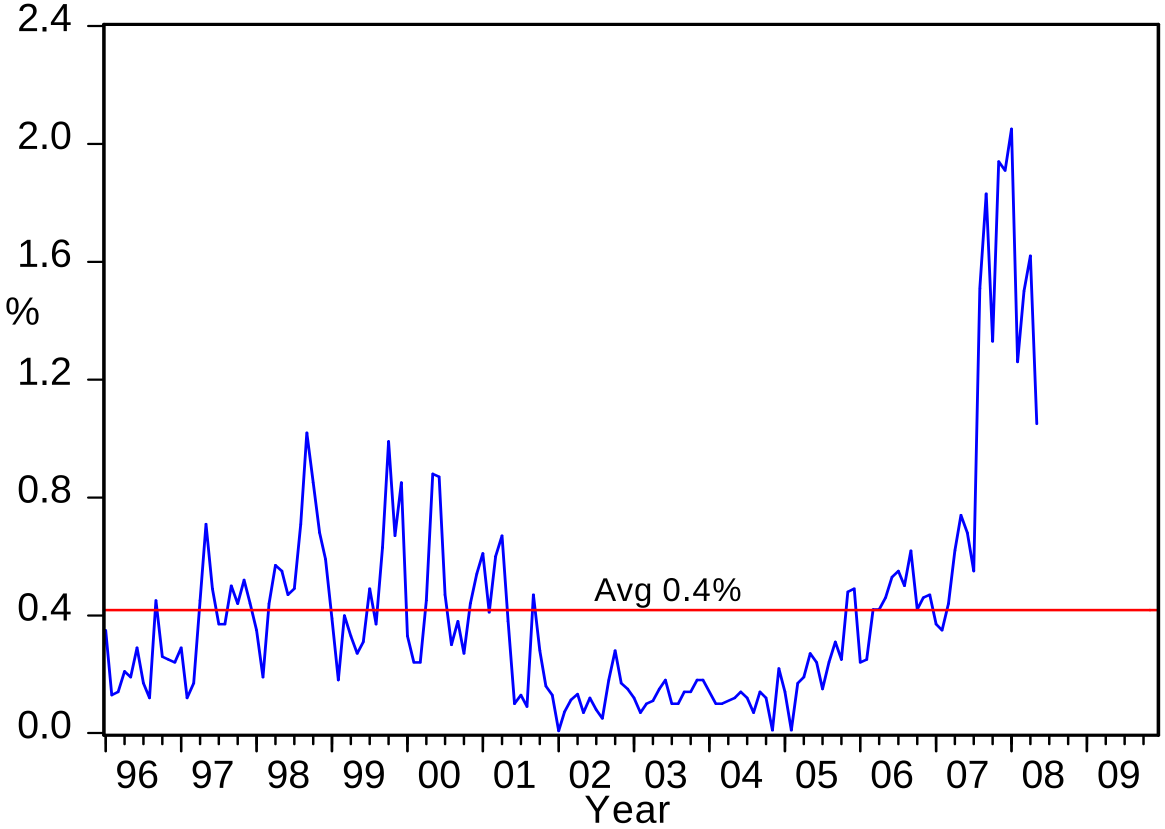
Asian Economic Perspective

	Year 2007	2008	2009
Real GDP Growth			
China	11.9	11.5	10.5
North East Asia (1)	9.6	8.0	7.7
South East Asia (2)	6.4	5.5	5.7
Consumer Price Inflation			
China	6.5	8.0	4.0
North East Asia (1)	3.9	6.0	3.4
South East Asia (2)	4.1	5.9	4.7

(1) China, Hong Kong, South Korea, Taiwan

(2) Indonesia, Malaysia, Singapore, Thailand and the Philippines

Eurodollar 90 Day Bills Minus 90 Day Treasury Yields (TED Spread)



After peaking at around 2.41% on 12 December, the TED spread has declined to 1.05% on 15 May. This is still much higher than the long term average of 0.4%.

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Term Auction Facility Provision of Discount Window Funds

Date	$US Billion
17 December 2007	20
20 December 2007	20
14 January 2008	30
28 January 2008	30
11 February 2008	30
25 February 2008	30
10 March 2008	50
25 March 2008	50
7 April 2008	50
21 April 2008	50
5 May 2008	75
19 May 2008	75

The FED's response has been to provide $US510bn of discount window credit over the period December to May. There is no sign this program is about to stop.

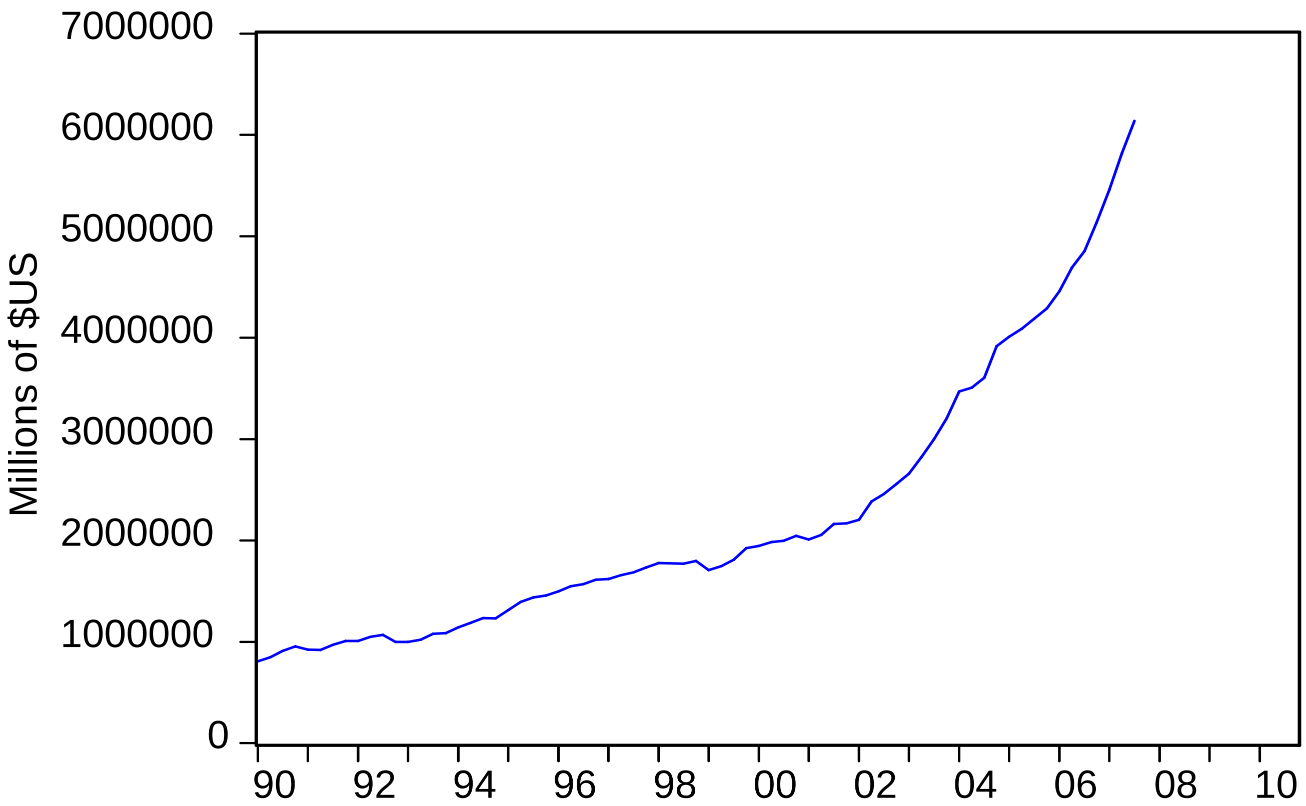
US Quarterly National Accounts

	QUARTER							
	3Q07	4Q07	1Q08	2Q08	3Q08	4QO8	1Q09	2Q09
GDP	4.9	0.6	0.9	0.2	1.7	-0.4	0.3	2.5
Fed Funds Rate	5.25	4.5	3.0	2.0	2.0	1.5	1.5	1.5

Source: ABN AMRO Morgans

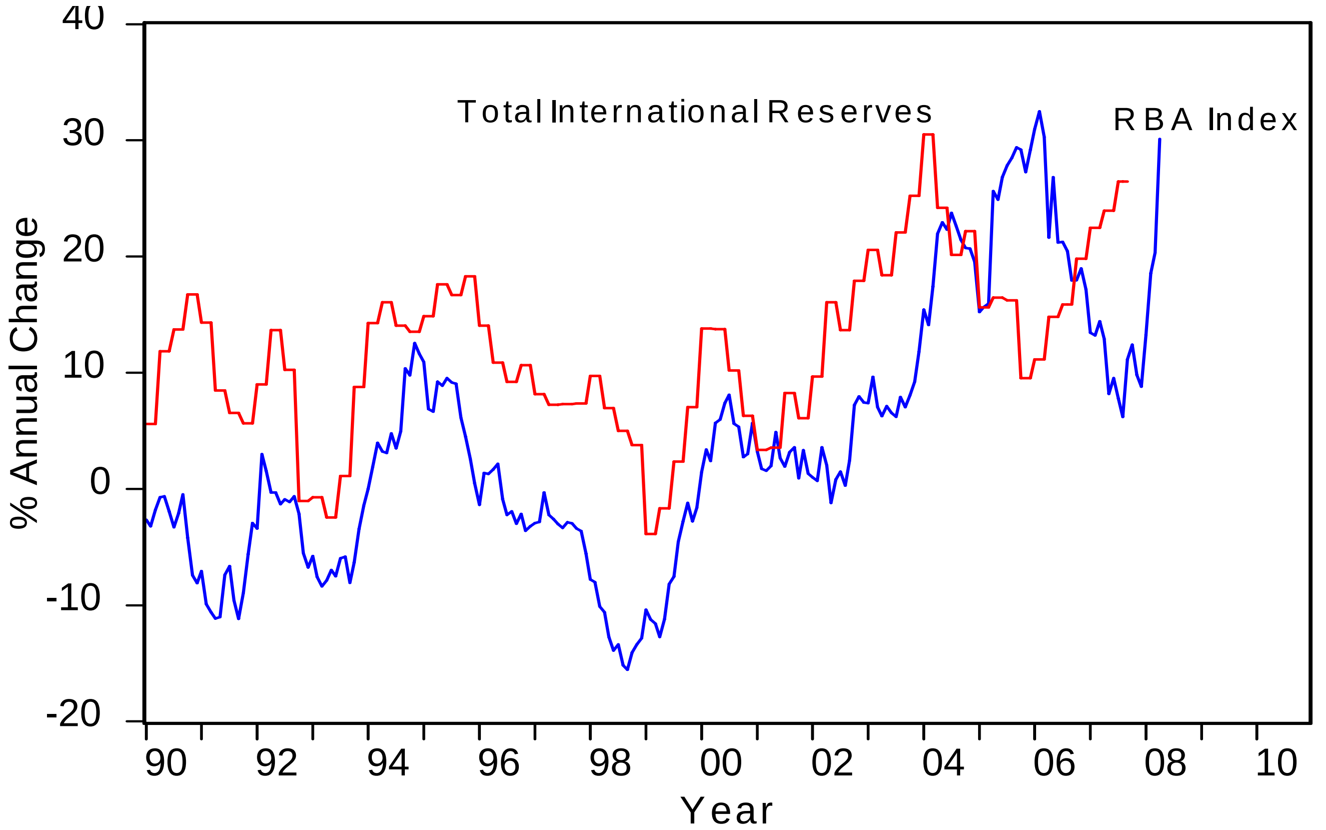
A sharp drop in earnings occurred because of a 4.3% drop in GDP growth in the December quarter. However, in the third quarter of 2008 GDP growth is expected to accelerate by 1.5%. If this occurs we might expect a modest rally in stocks in the fourth quarter of 2008. Unfortunately the economy remains too weak to support a sustained broad rally until well into 2009.

Total International Reserves – 1990 to 2008



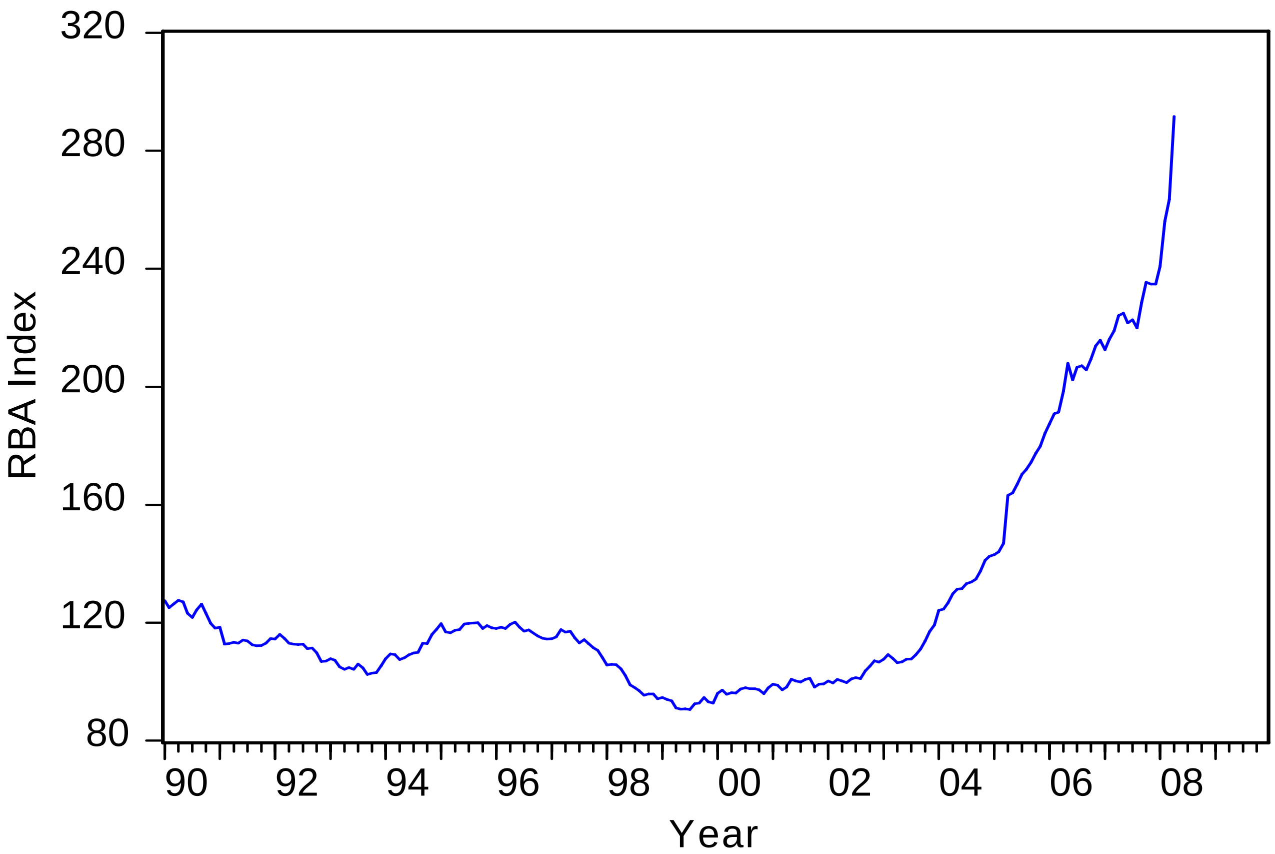
Total International Reserve growth has accelerated during this decade.

Commodity Inflation Versus Growth in International Reserves – 1990 to 2008



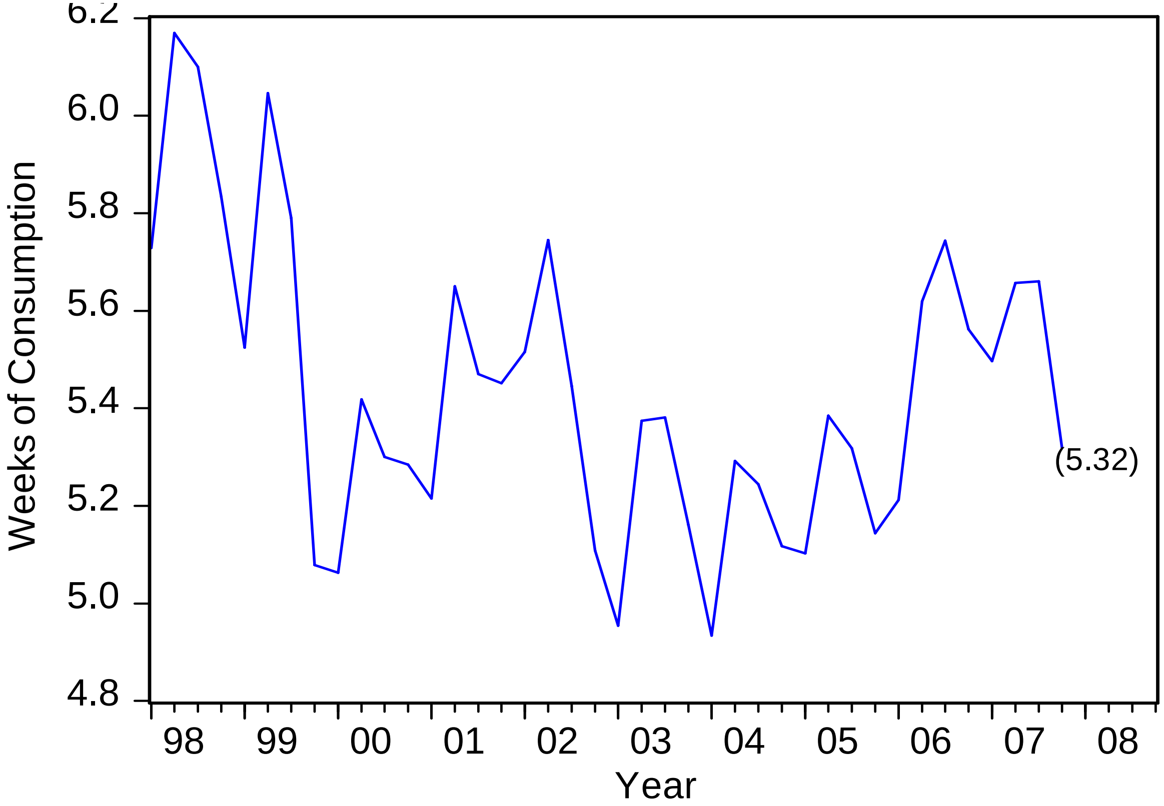
The growth rate of Australian export prices re-accelerated in 2008 following the lead period by accelerating total international reserves.

RBA Index of $US Commodity Prices – 1990 to 2008



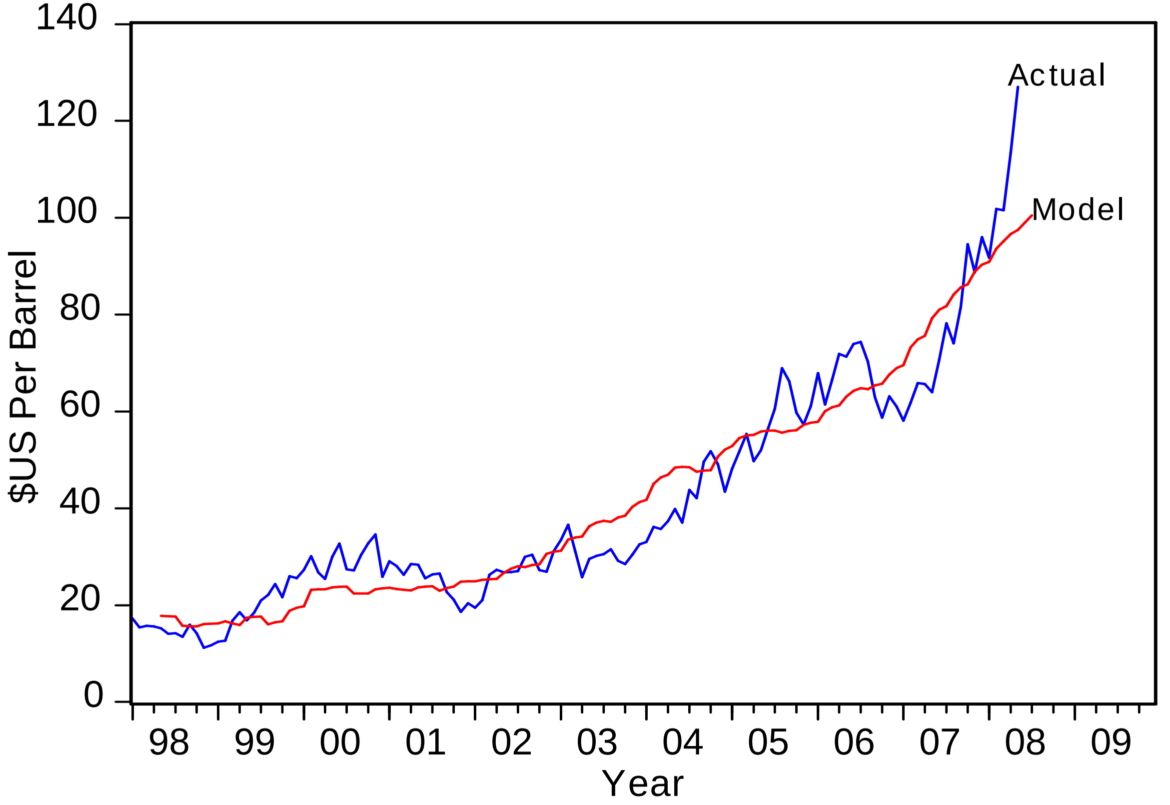
Australian export prices are now moving up in an almost vertical ascent.

IEA – Closing Stocks of Refined Petroleum Products (in weeks of consumption)



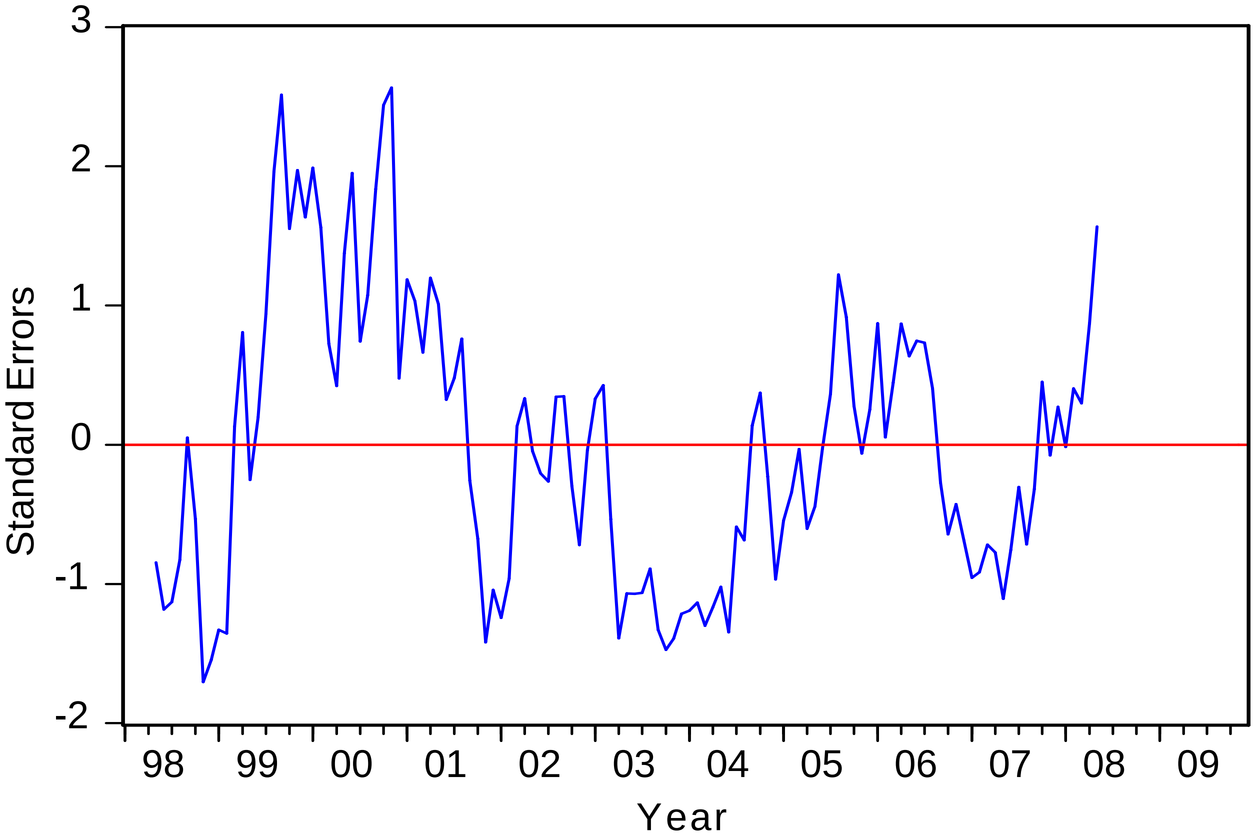
Stocks of refined petroleum products fell sharply in the final quarter of 2007 as imports fell more rapidly (-5.1%) than consumption (-1%).

A Model of the Oil Price - 1998 to 2008



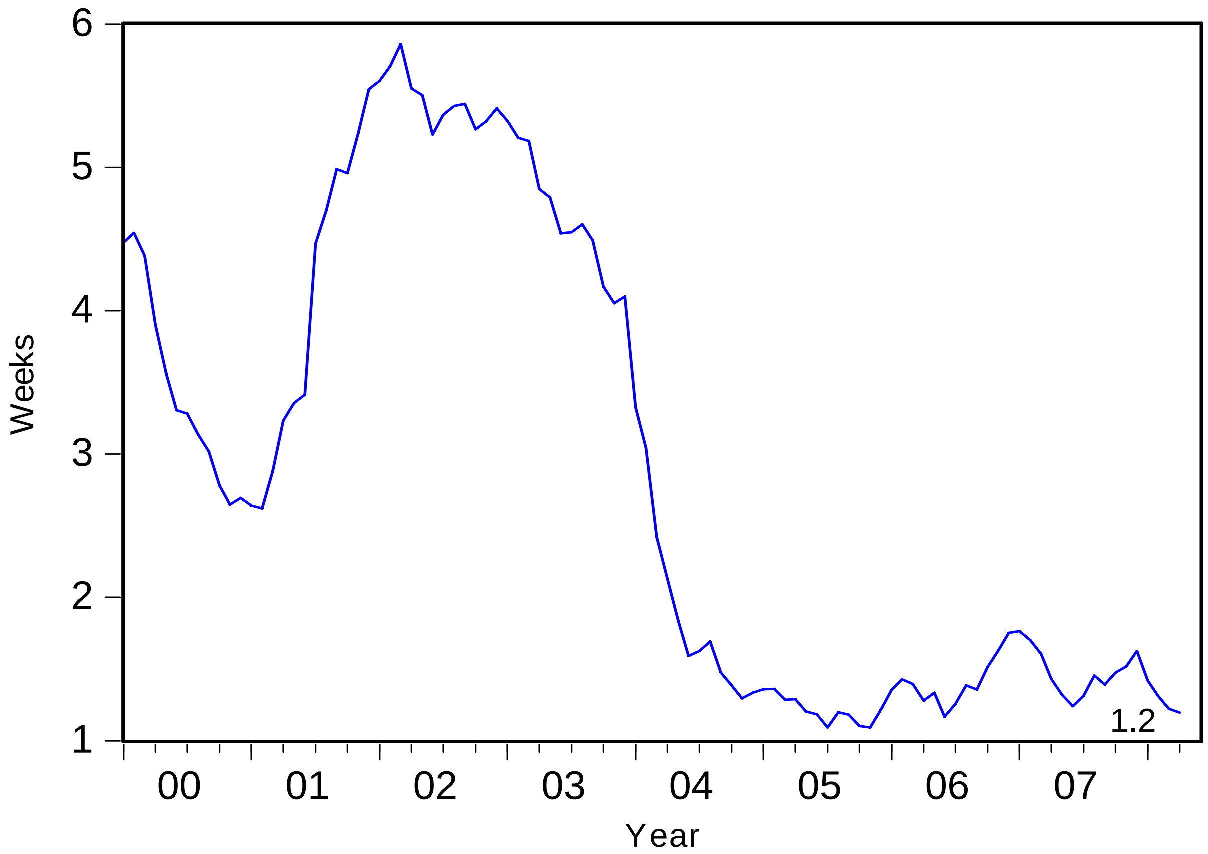
The equilibrium price of West Texas Intermediate Grade is now $US97.51 per barrel. This is $US29.46 below the traded price on 20 May of $US127.05. This is 1.6 standard errors in excess of fair value.

Oil Overbought / Oversold Indicator



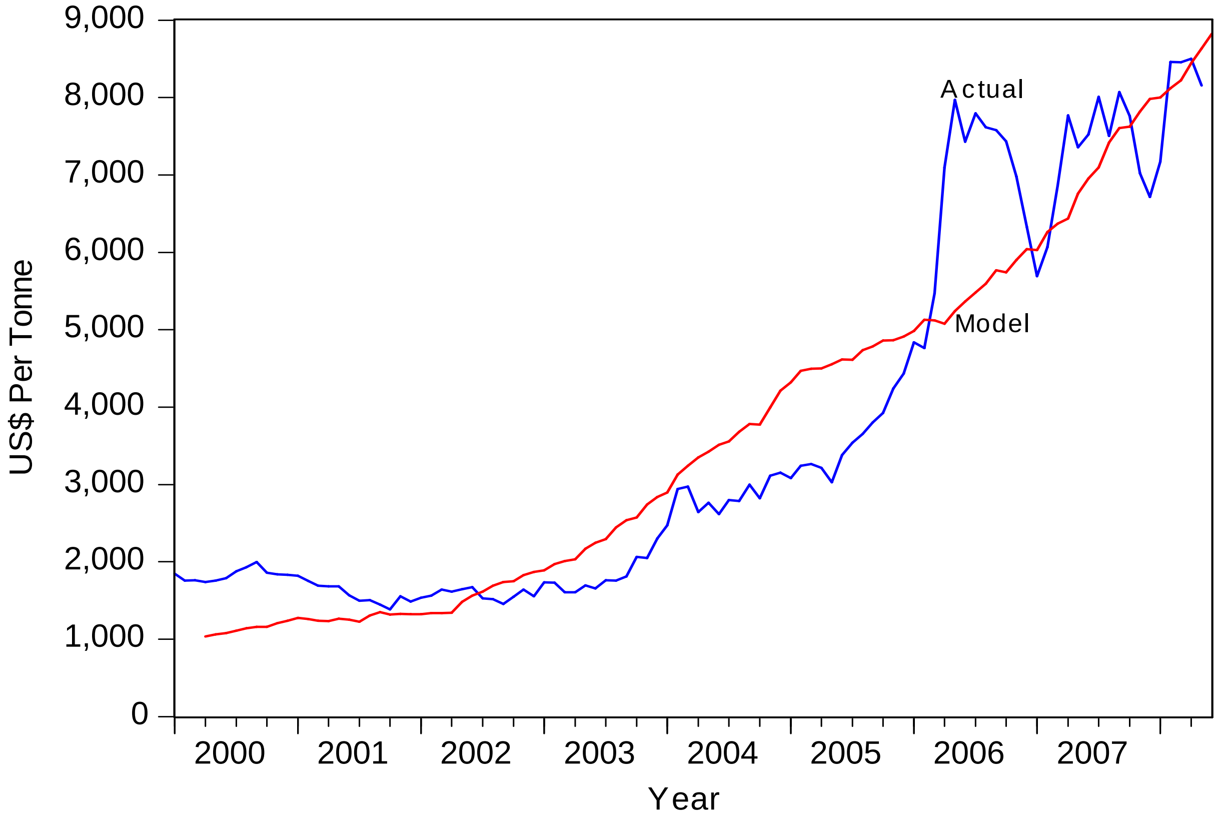
Oil is now 1.6 standard errors in excess of our model estimate. It has overshot the peak levels of overvaluation of 2005 but is not as high as the 2.5 standard errors of overvaluation it saw in 2000. Should oil put in a peak in a similar level as in 2000, it would begin building a top at around $US145 per barrel.

Copper Closing Stocks (Western World, Quarterly) - 2000 to 2007



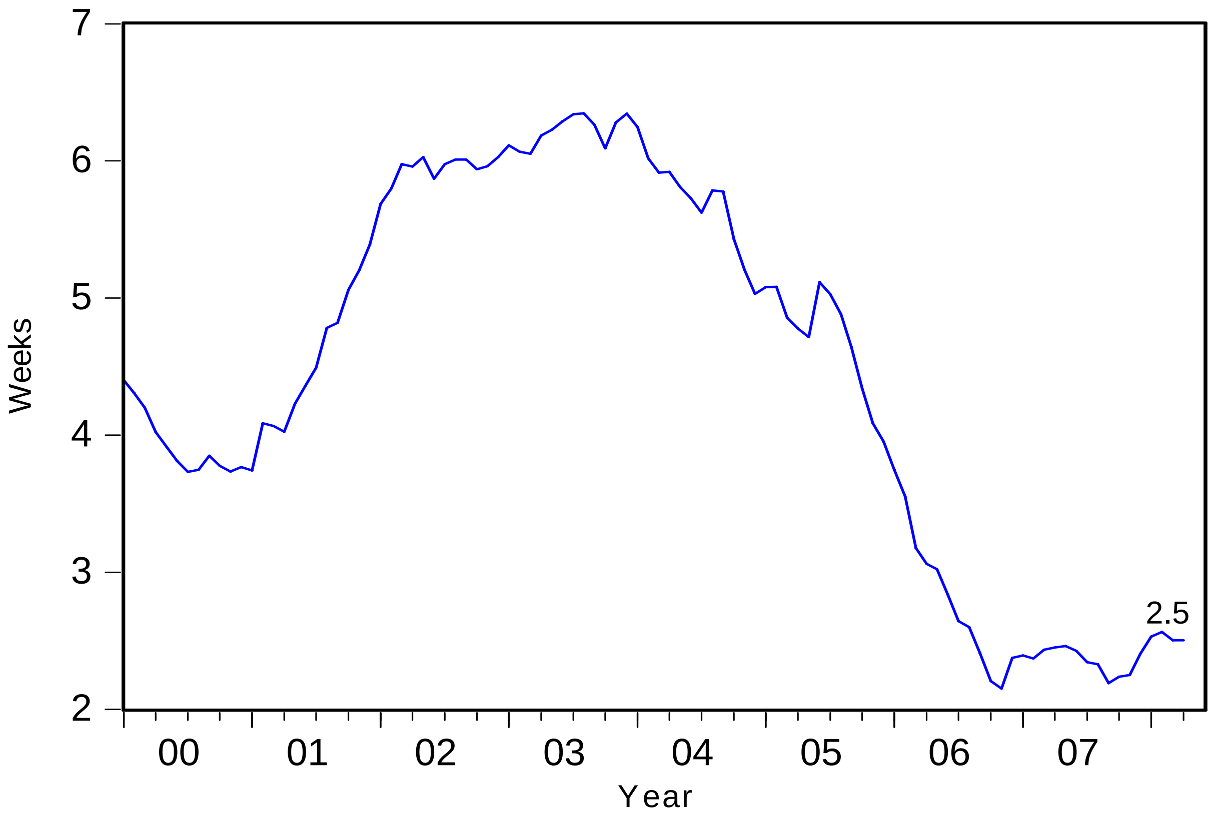
After rising in late 2007, copper stocks have begun to decline again in calendar 2008. The current stocks to consumption ratio of 1.2 weeks consumption is only slightly higher than the low in 2005.

A Model of the Copper Price – 2000 to 2008



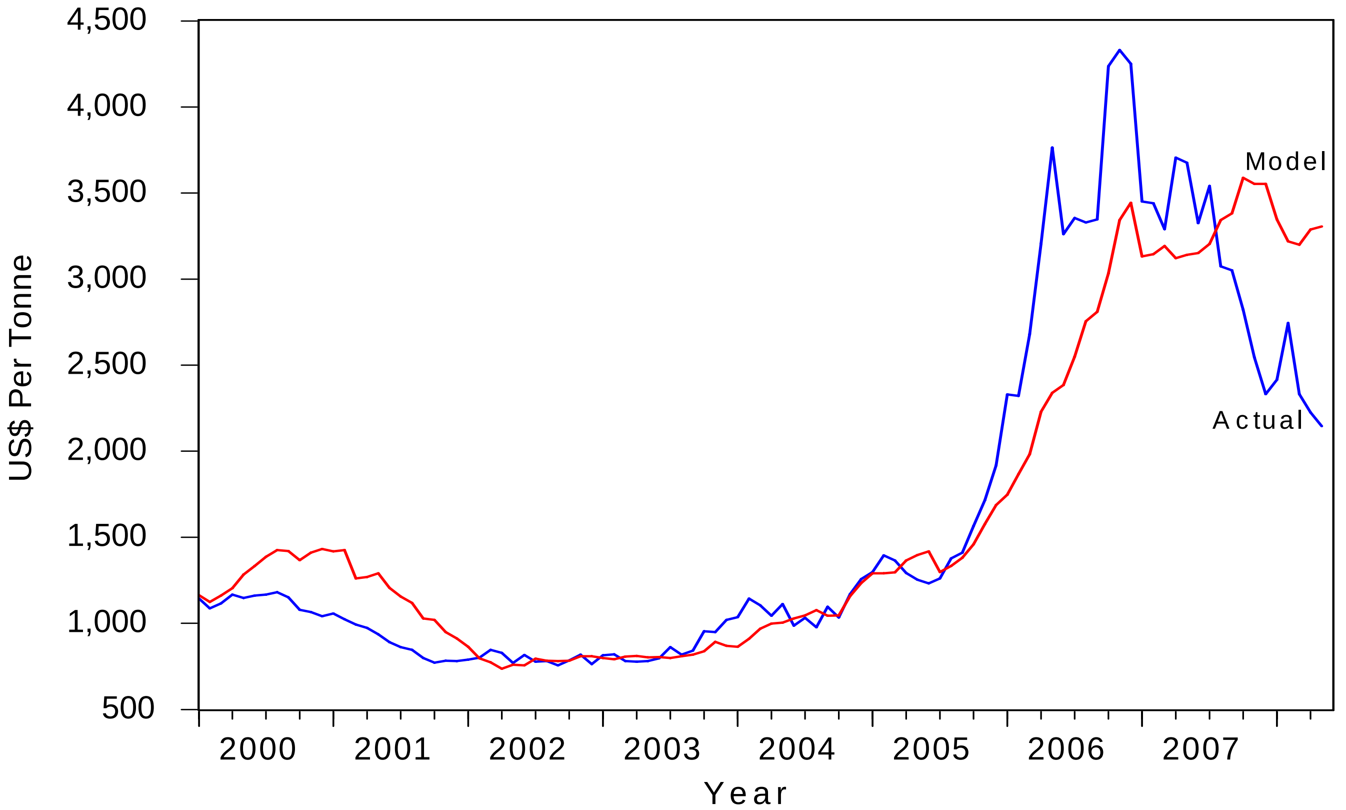
Our model explains 87.2% of monthly variation. The copper price at $US8,155 per tonne on 27 May is $US481 per tonne below the equilibrium price of $US8,636. Copper is slightly cheap.

Zinc Closing Stocks (Western World, Monthly) – 2000 to 2008



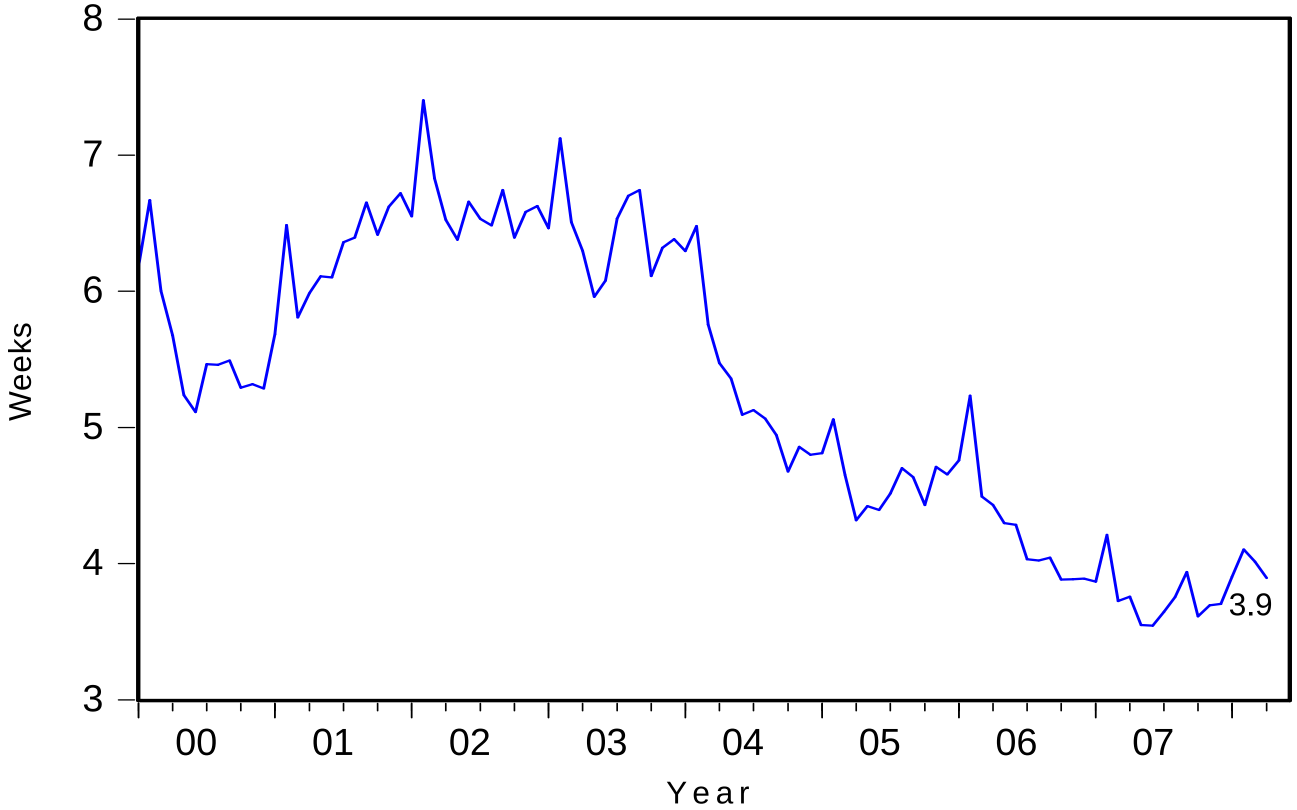
Zinc stocks rose slightly in the second half of 2007. This rise generated an exaggerated selloff in the zinc price. Zinc prices appear to have stabilised and have begun a slight decline.

A Model of the Zinc Price – 2000 to 2008



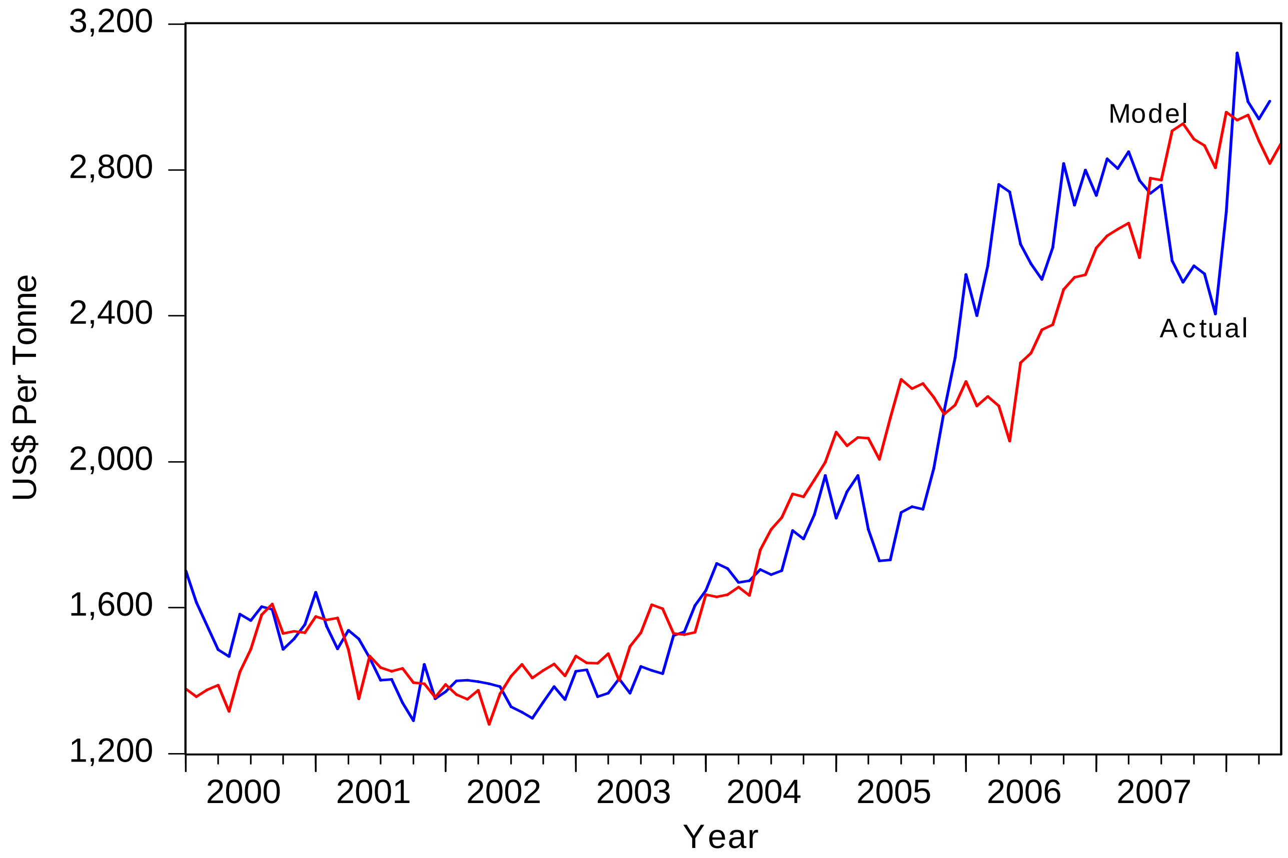
Our model explains 81% of monthly variation of the zinc price. On 27 May, the zinc price at $US2,145 per tonne was $US1,161 below fair value of $US3,306. The sell off has been overdone. Zinc is outrageously cheap.

Aluminium Closing Stocks (Total World, Monthly) 2000 to 2008



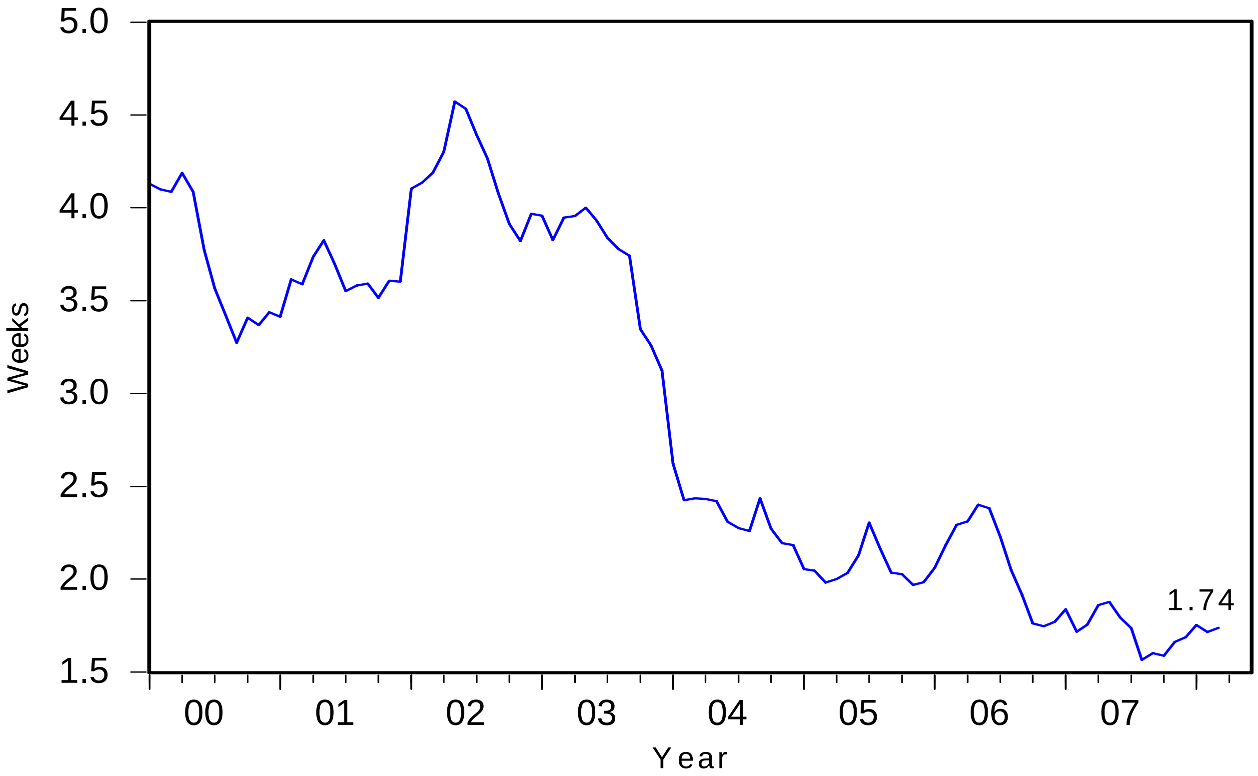
Aluminium stocks rose slightly in late 2007. They have now begun to decline.

A Model of the Aluminium Price – 2000 to 2008



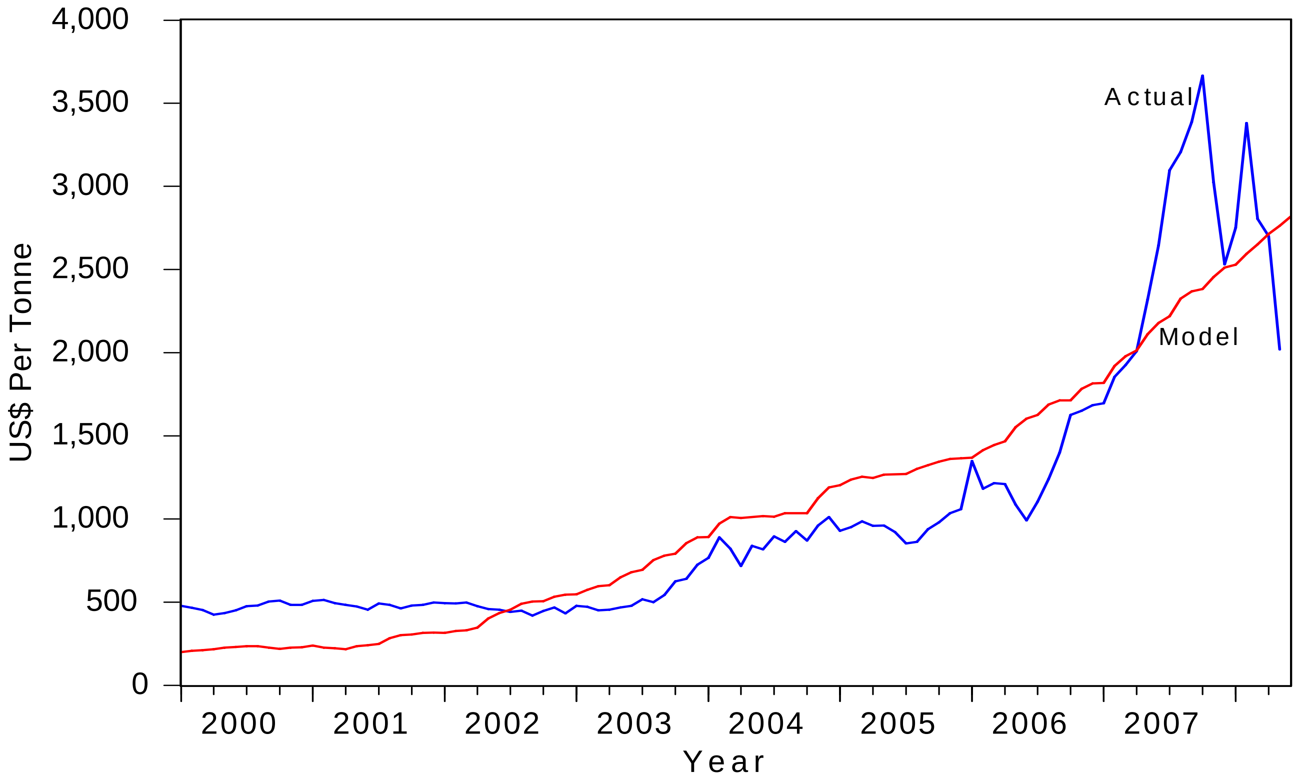
Our model explains 86.5% of monthly variation. On 27 May, the aluminium price at $US2,989 per tonne was $US171 in excess of the equilibrium price of $US2,818. Aluminium is modestly overpriced.

Lead Closing Stocks (Western World, Monthly) – 2000 to 2008



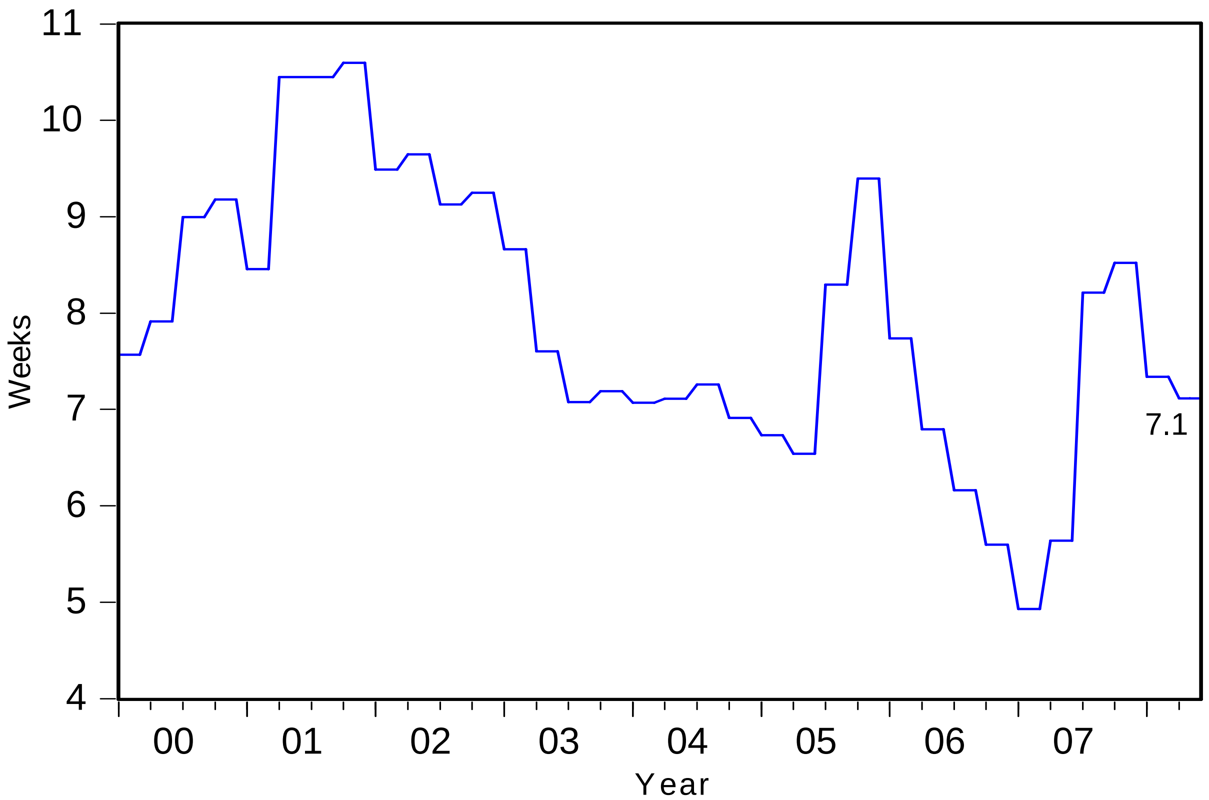
After bottoming out in mid 2007, lead stocks began to rise in the second half of 2007. This slight increase in stocks generated a collapse in the price.

A Model of the Lead Price – 2000 to 2008



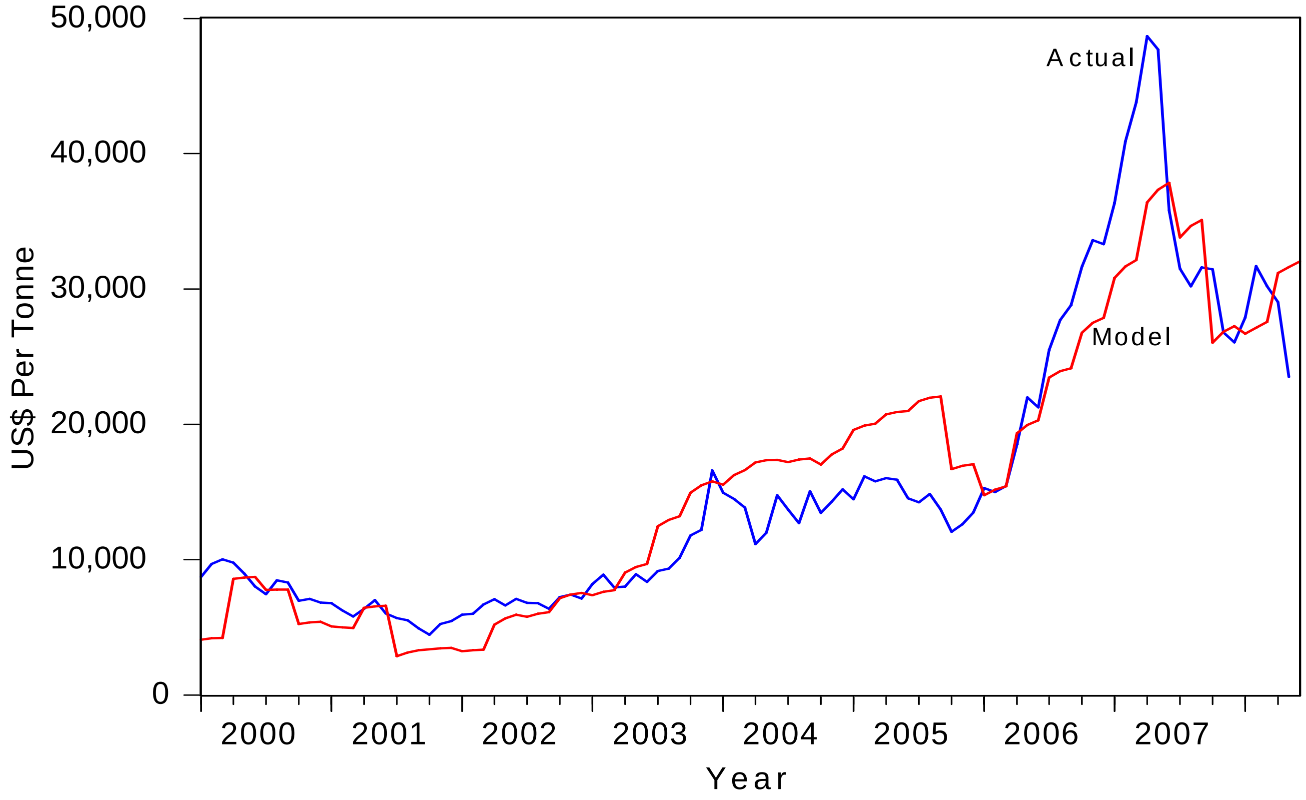
Our model explains 83% of monthly variation. At US$2,020 per tonne on 27 May, lead is US$742 below the equilibrium price of $US2,762. Lead has now collapsed for a second time in the last year. Lead is now genuinely very cheap.

Nickel Closing Stocks (Total World, Quarterly) – 2000 to 2007



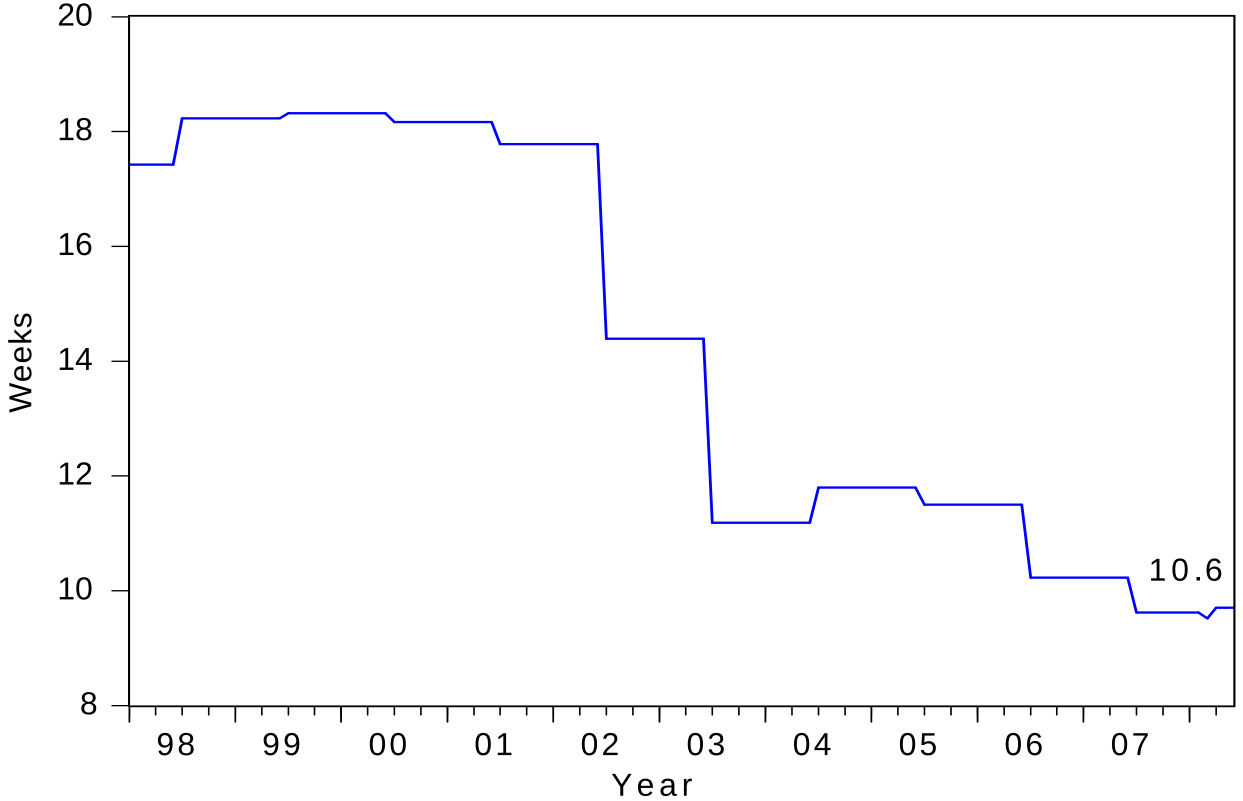
World nickel stocks rose in 2007 because of the rise in prices at that time. Falling prices since have allowed demand to increase and stocks to fall. This increases the equilibrium price of nickel.

A Model of the Nickel Price – 2000 to 2008



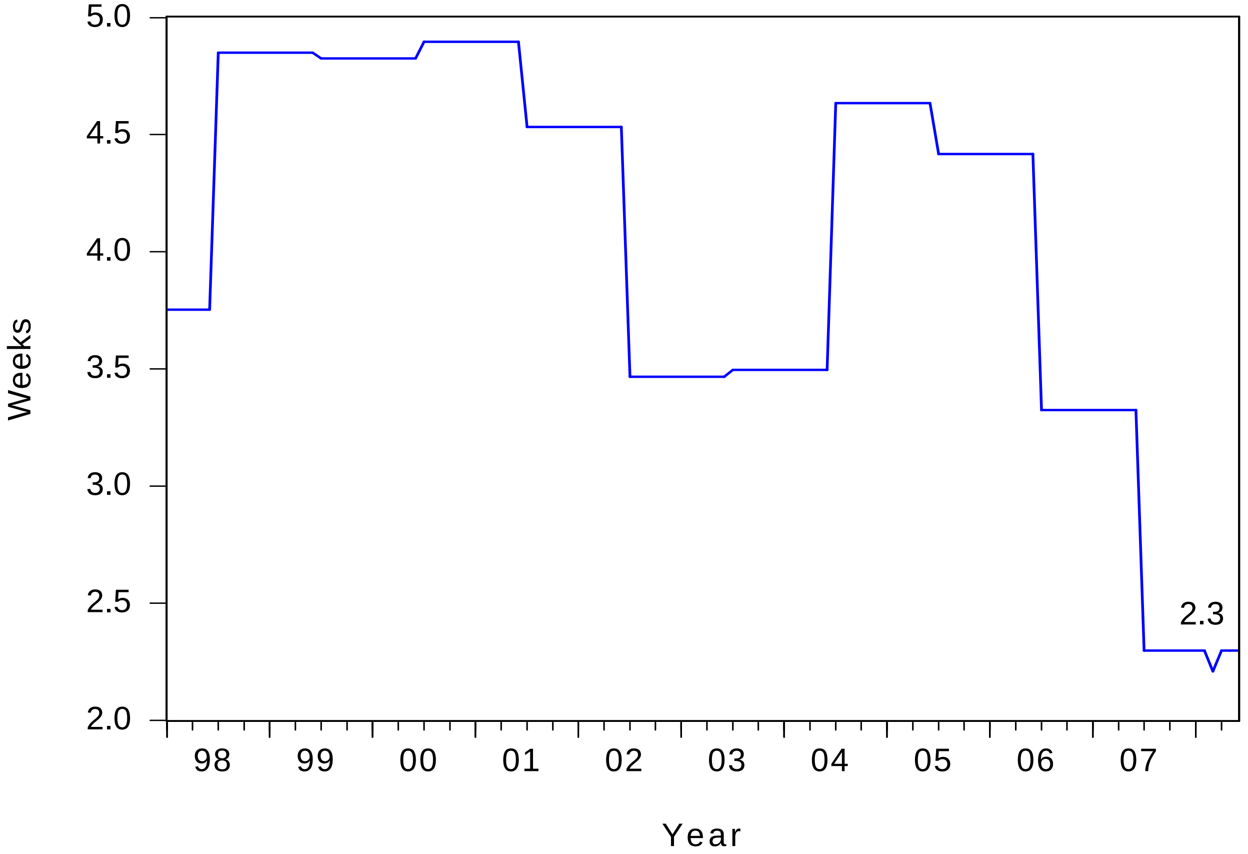
Our model explains 85.5% of monthly variation in the nickel price. On 27 May, the nickel price at $US23,510 per tonne is $US8,100 per tonne lower than our equilibrium price of $US31,610 per tonne. Nickel is cheap here enough to be an outright BUY.

Global Ending Wheat Stocks (weeks of consumption)



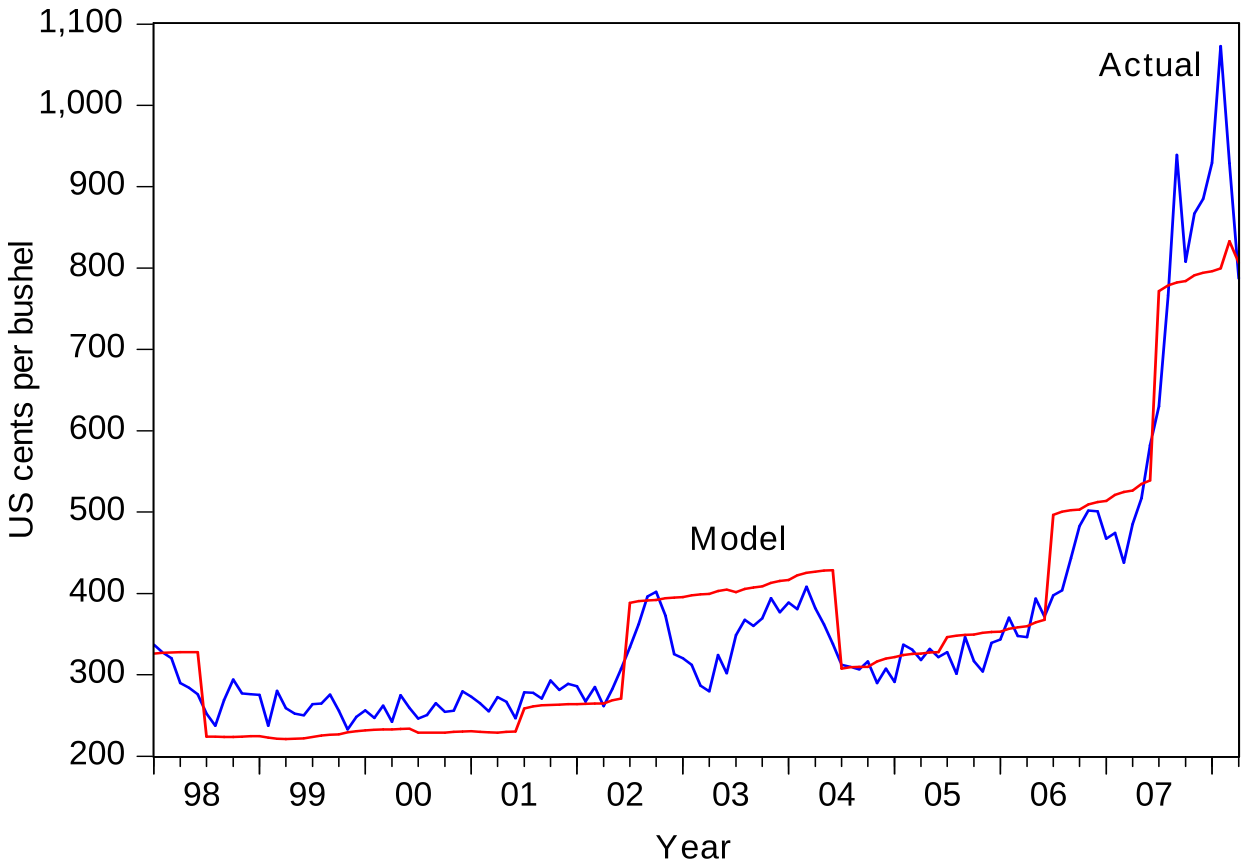
Global wheat stocks are the lowest since 1948.

Wheat Major Exporters Stocks (weeks of global consumption)



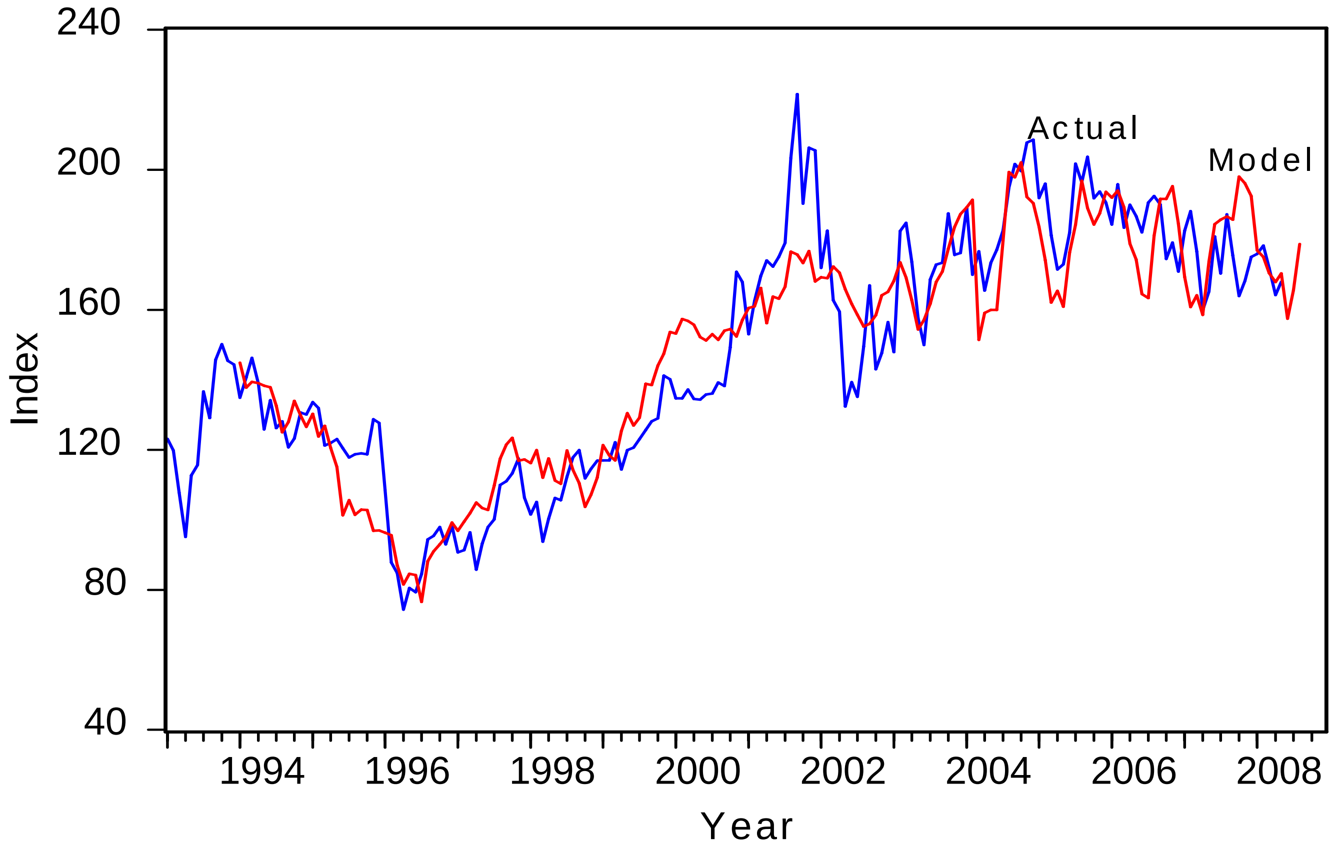
Wheat stocks of major exporters are the lowest for the sample period of 10 years.

A Model of the $US Wheat Price 1998 to 2008



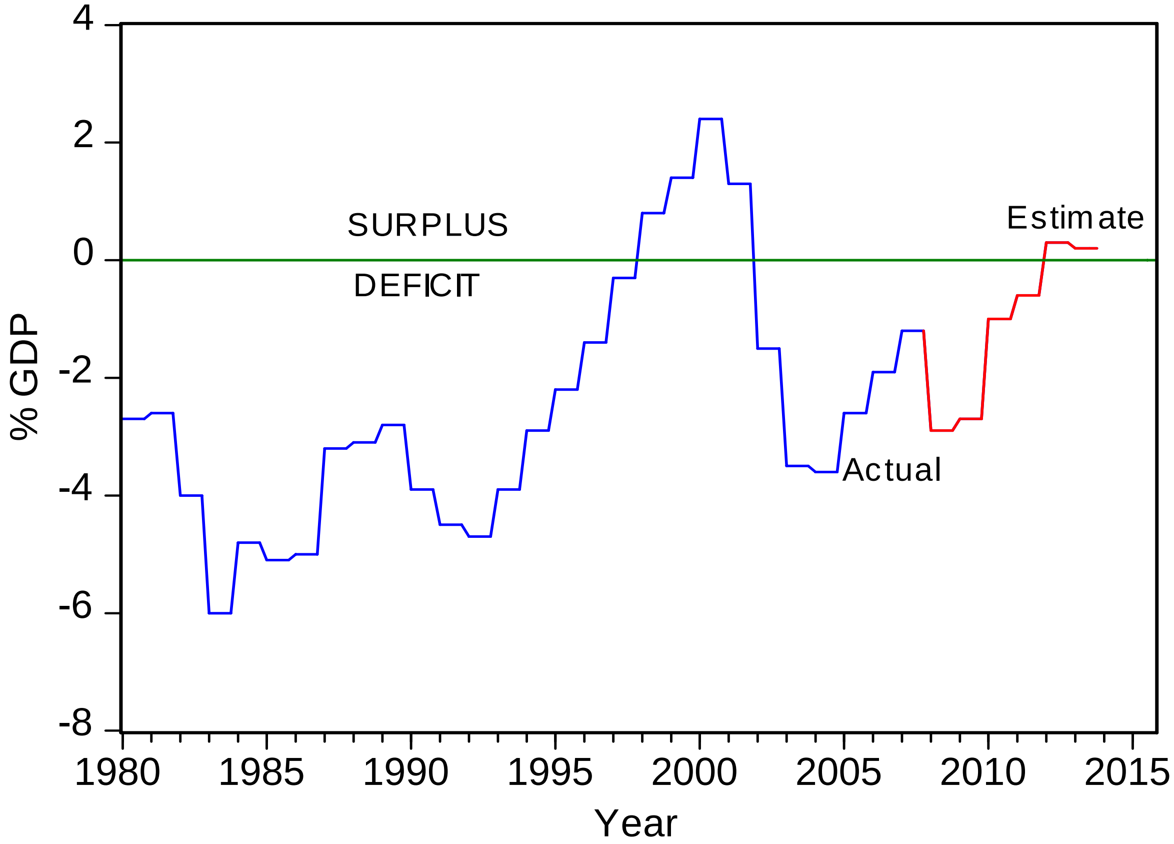
Our model explains 89% of monthly variation of the $US wheat price. At $US7.87 per bushel on 20 May, wheat is US19.5 cents below fair value of $US8.07.

Model of the Queensland Cattle Index



US grain prices interact with US livestock numbers to produce a demand for grass fed beef shown as the feeder cattle price. This leads the Queensland Cattle Index by 3 months. Our model explains 84.7% of variation. The QCMI should rise from 168 in May to 178 in August.

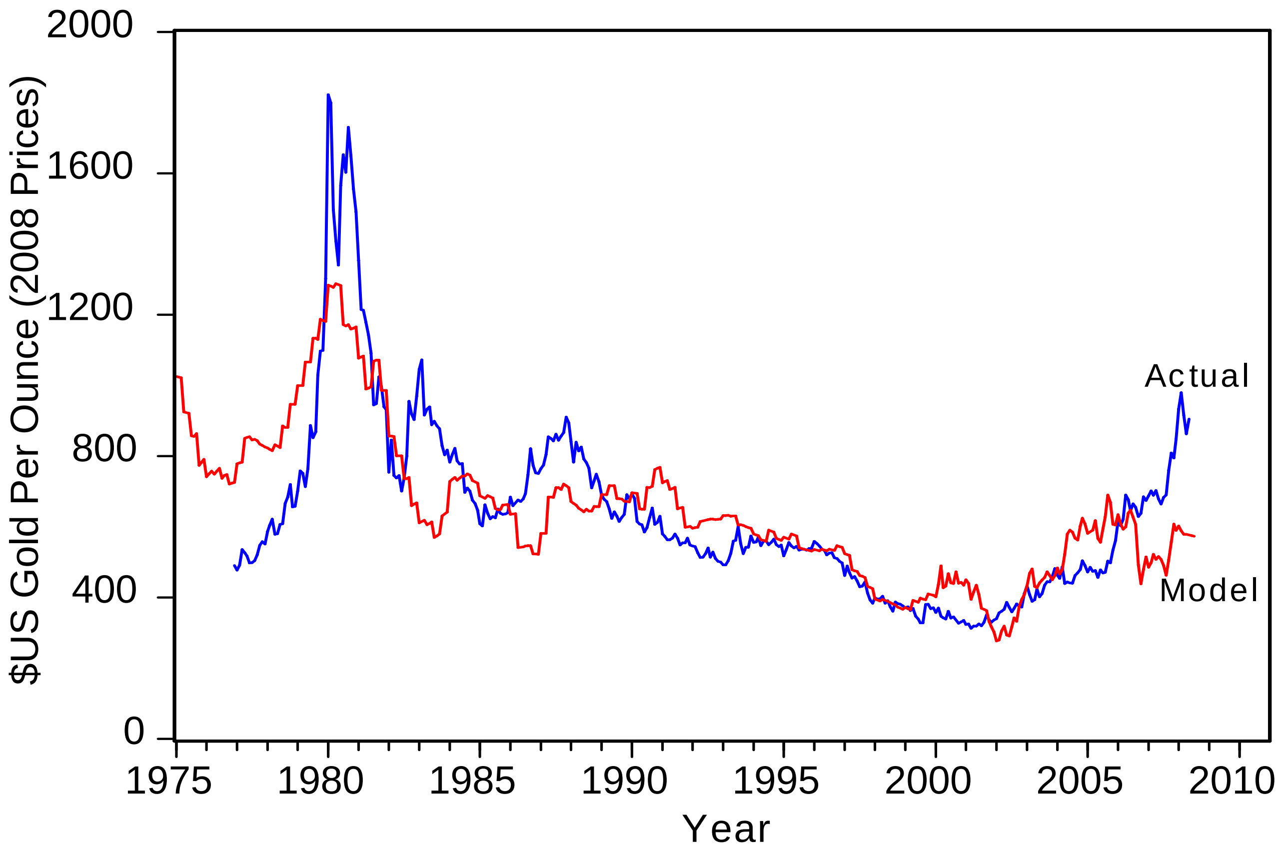
US Federal Budget Balance – 1980 to 2013



Source: Whitehouse Office of Management and Budget

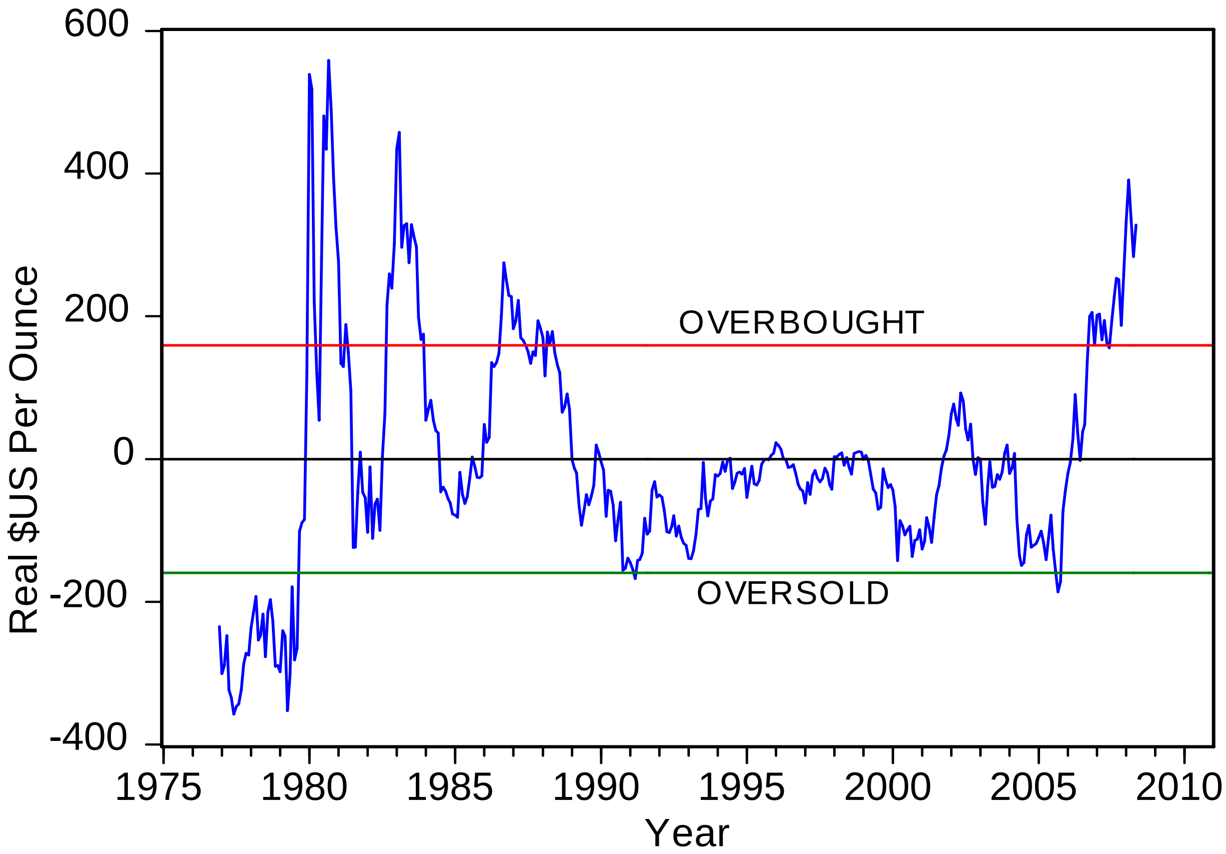
The US budget deficit should worsen to 2.9% of GDP in 2008 as the US economy weakens. There is further downside risk in this estimate to 4% of GDP.

A Model of the Real Gold Price – 1976 to 2008



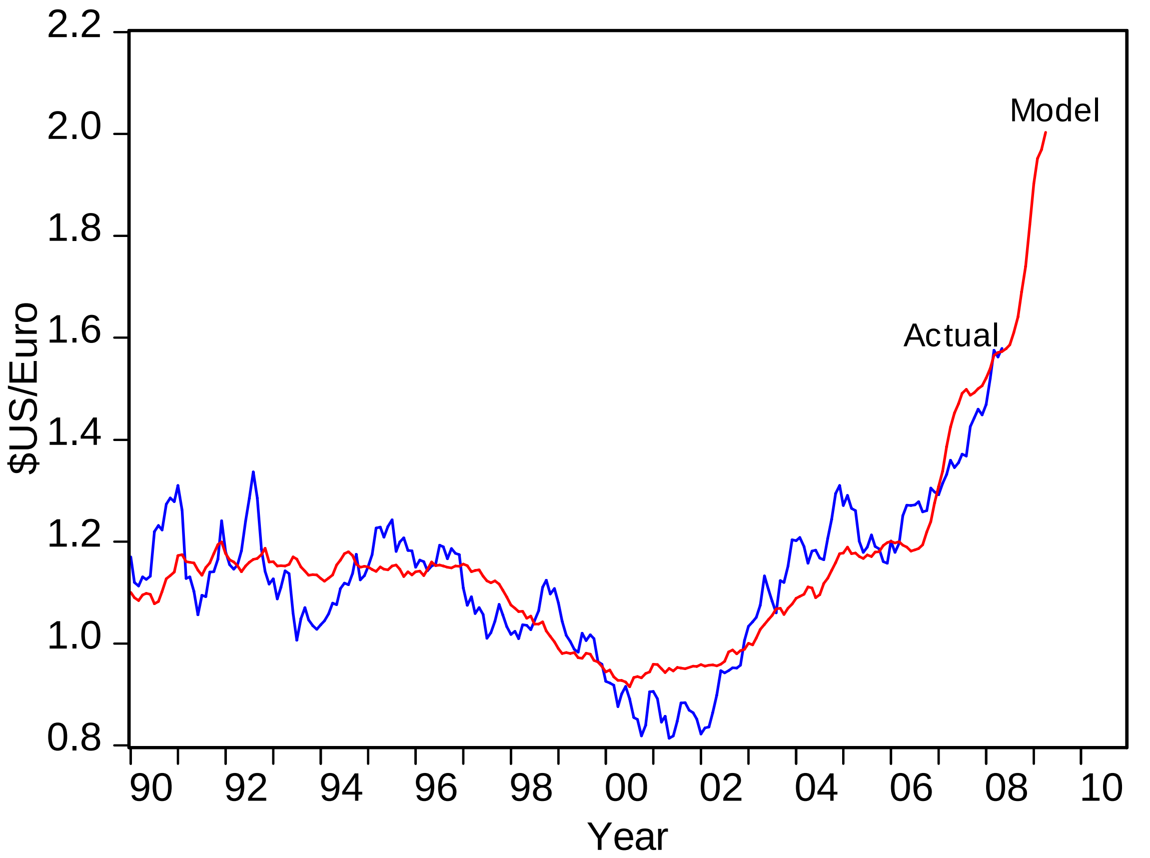
Our model is based on the US budget balance and US headline inflation. The equilibrium price is now $US577 per ounce or $US327.8 per ounce below the actual traded price on 21 May of $US905 per ounce.

Gold Overbought/Oversold Indicator



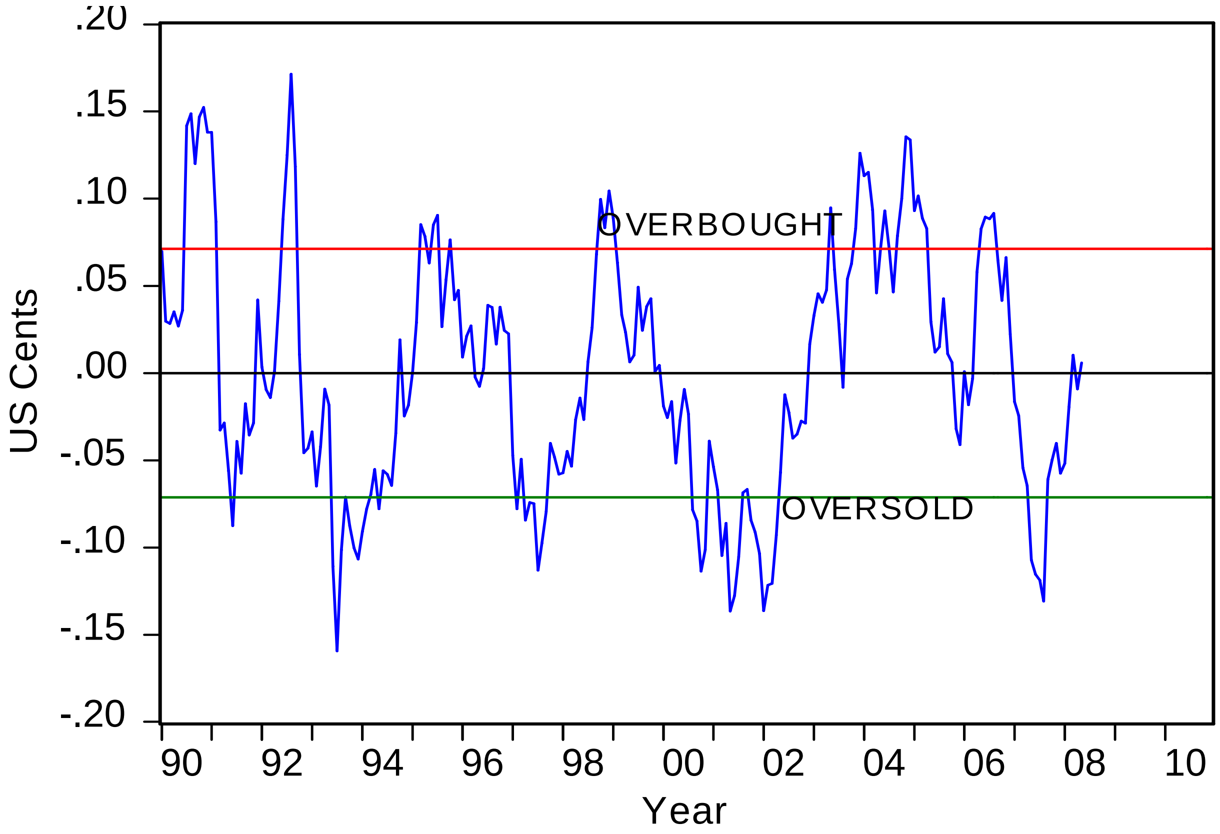
Gold is now as overvalued as it was in 1983 but not as overvalued as it was in 1980.

Model of the Euro – 1990 to 2008



The $US should continue to fall over the year ahead. The fall accelerates in the second half. Our model of the Euro reaches $US2.0 in April 2009.

$US/Euro Overbought/Oversold Indicator



At $US1.579 on 21 May the Euro is at almost exact fair value of $US1.57314.

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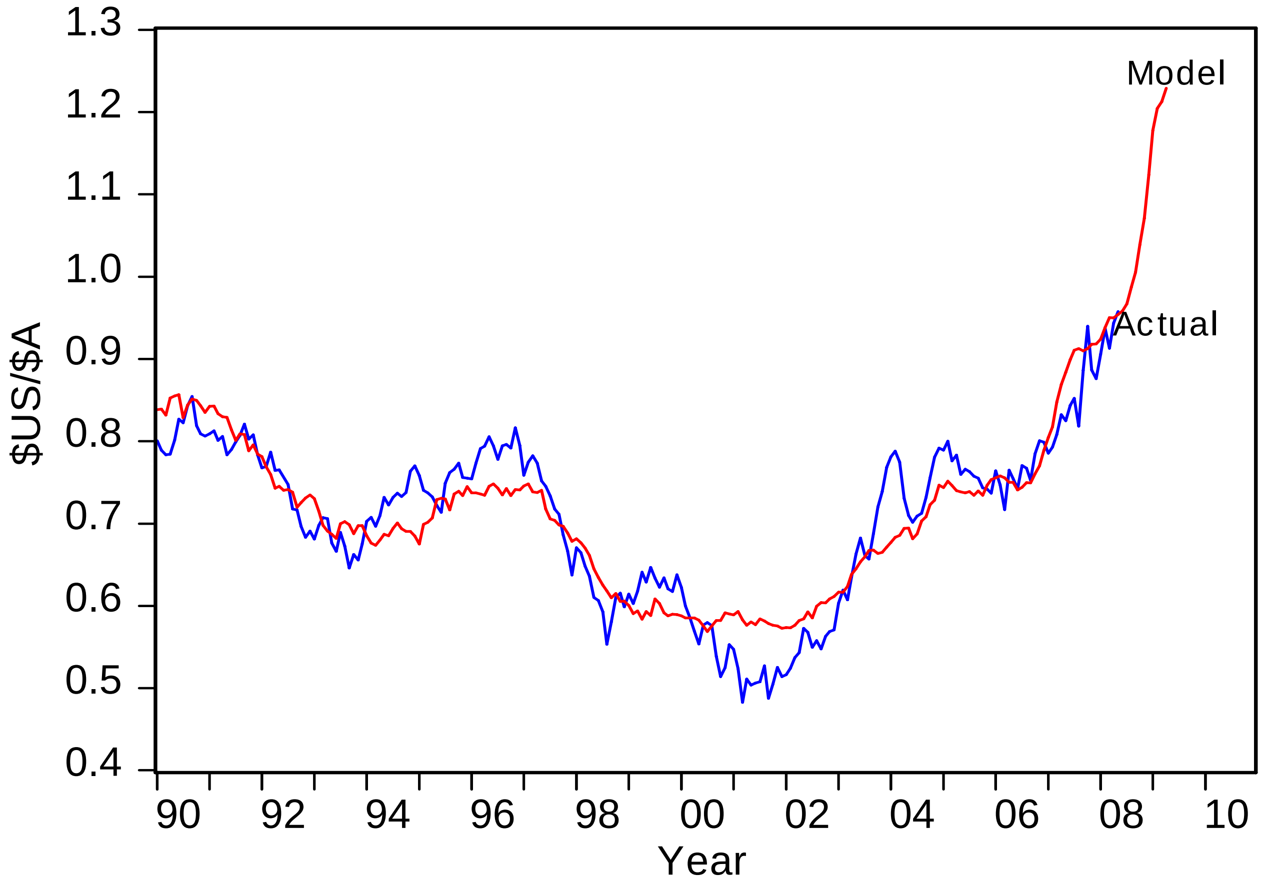
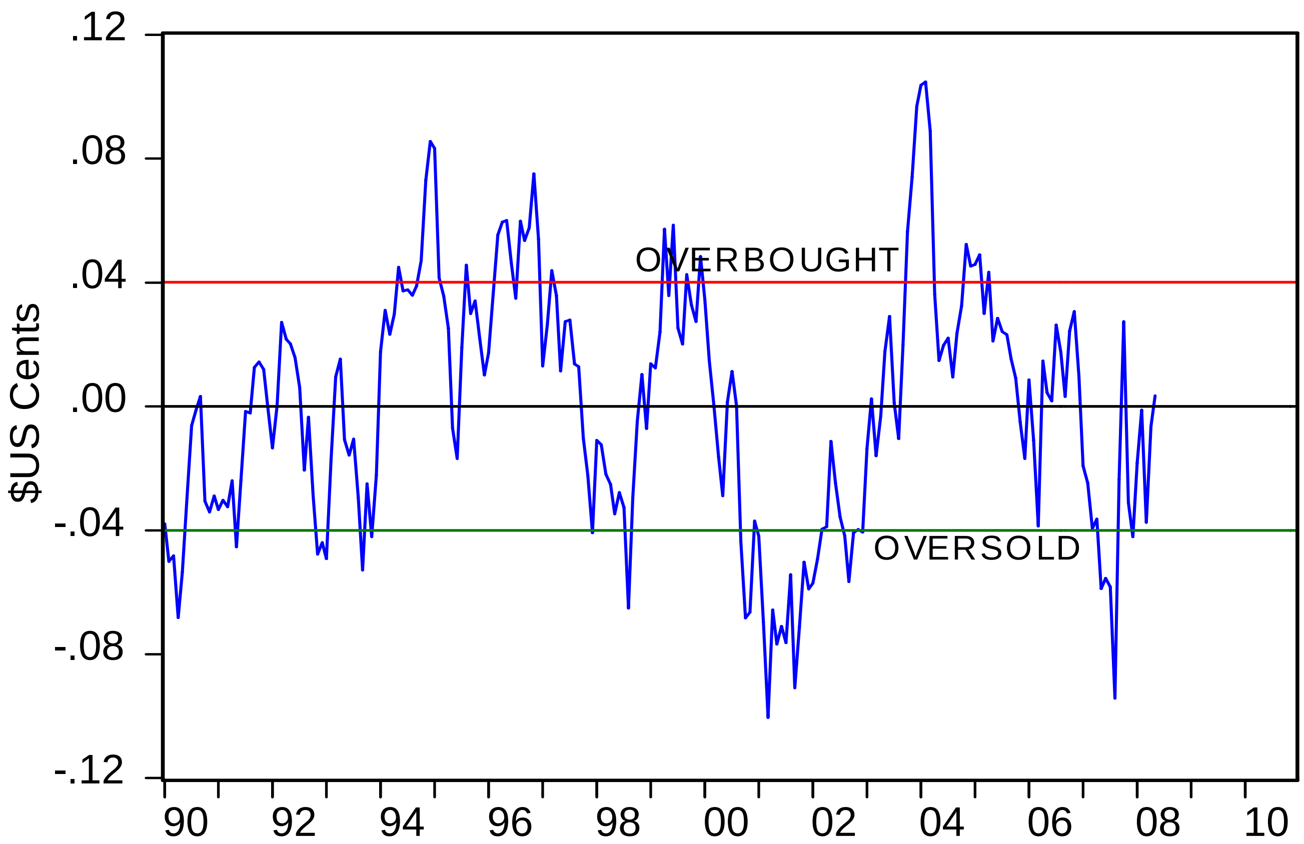
Model of the $US/$A - 1990 to 2008



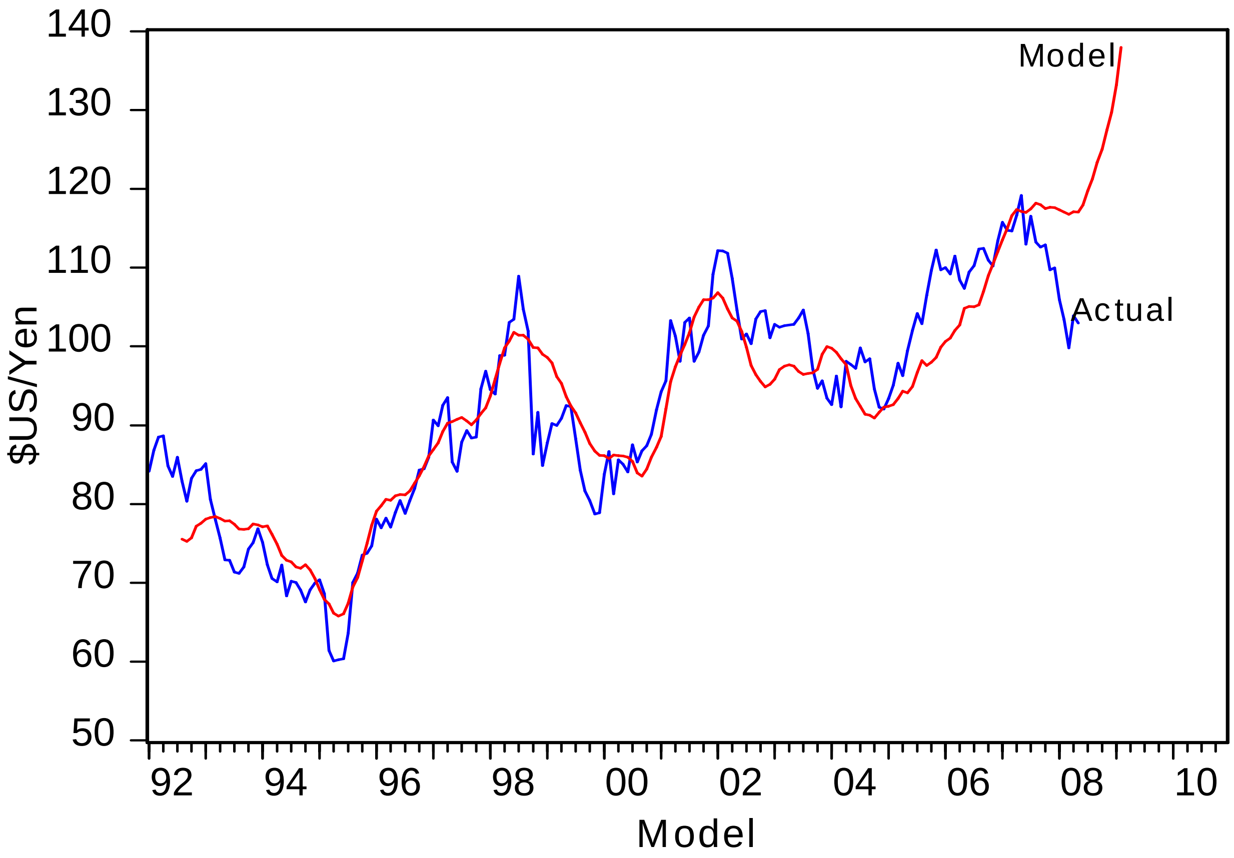
As the $US declines against the Euro, the $A should also rise. Our model rises to $US1.22 by April 2009.

$US/$A Overbought/Oversold Indicator



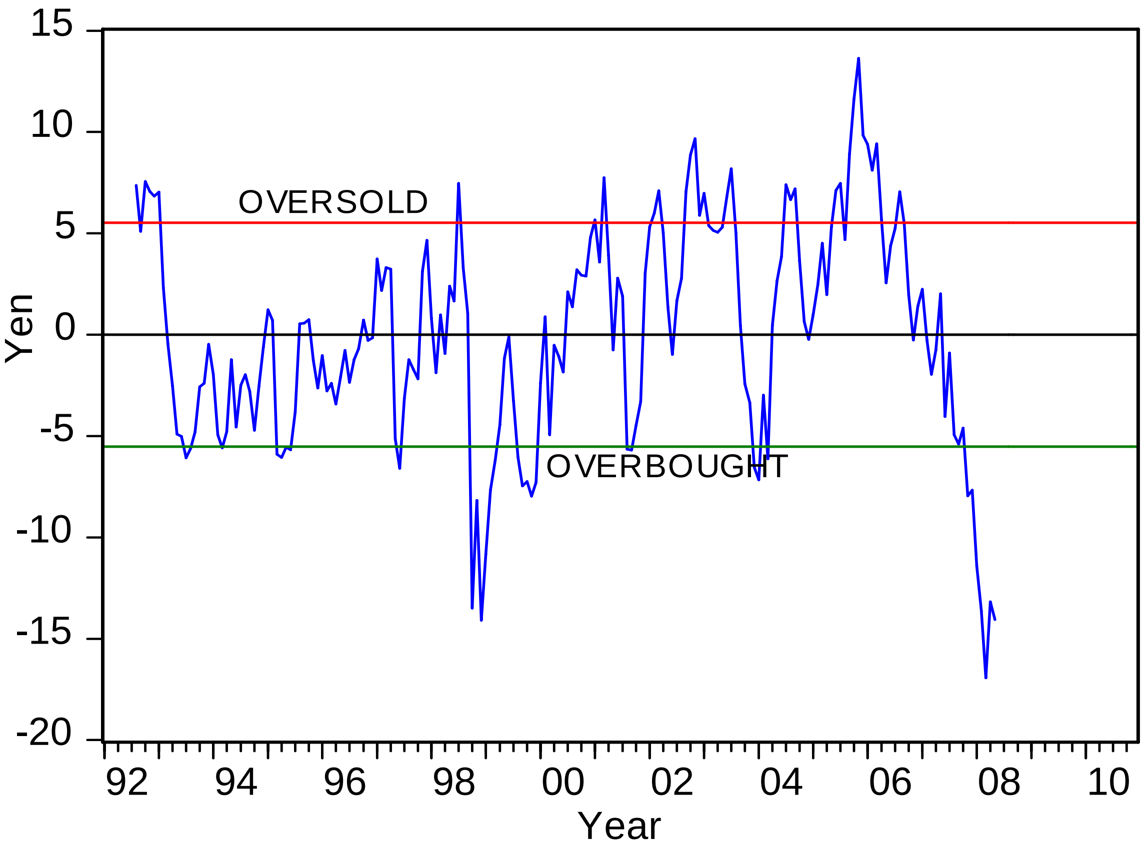
At US95.74 cents on 21 May, the $A is at almost exact fair value of US95.39 cents.

Model of the Real Yen/$US



Our model is based on the oil price, the current account and bond differential. Our model suggests a bear market for the Yen. This is a terms of trade argument with rising oil prices pushing down the Japanese terms of trade.

Yen/$US Overbought/Oversold Indicator



Our model explains 85% of monthly variation of the Yen/$US. At 102.98 Yen on 21 May, the $US is 14 Yen below fair value of 117.035 Yen. The Yen is the most overbought since the Russian debt crisis of 1998.

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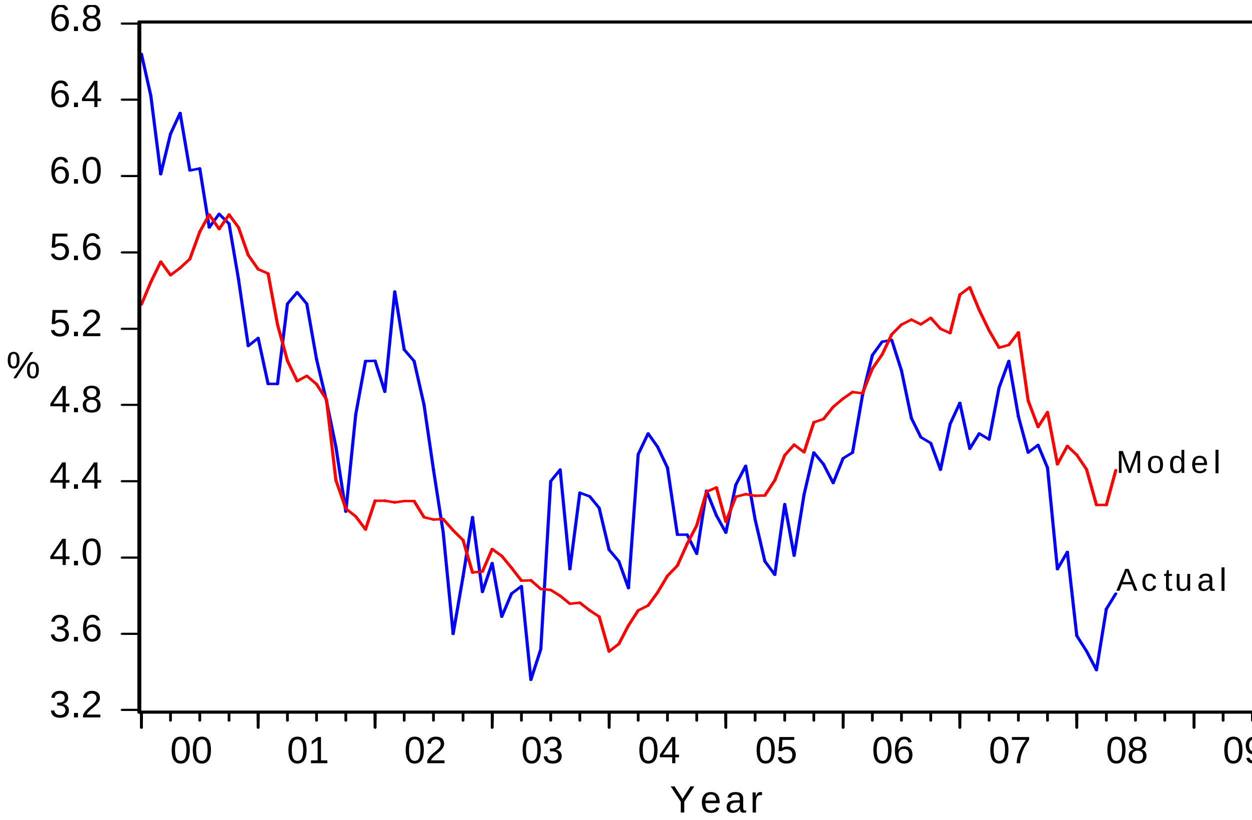
US Ten Year Bond Yield Versus Appropriate Model Value – January 2000 to May 2008



US Ten Year Bond yields on 21 May at 3.81% were 65 basis points below appropriate yield of 4.46%.

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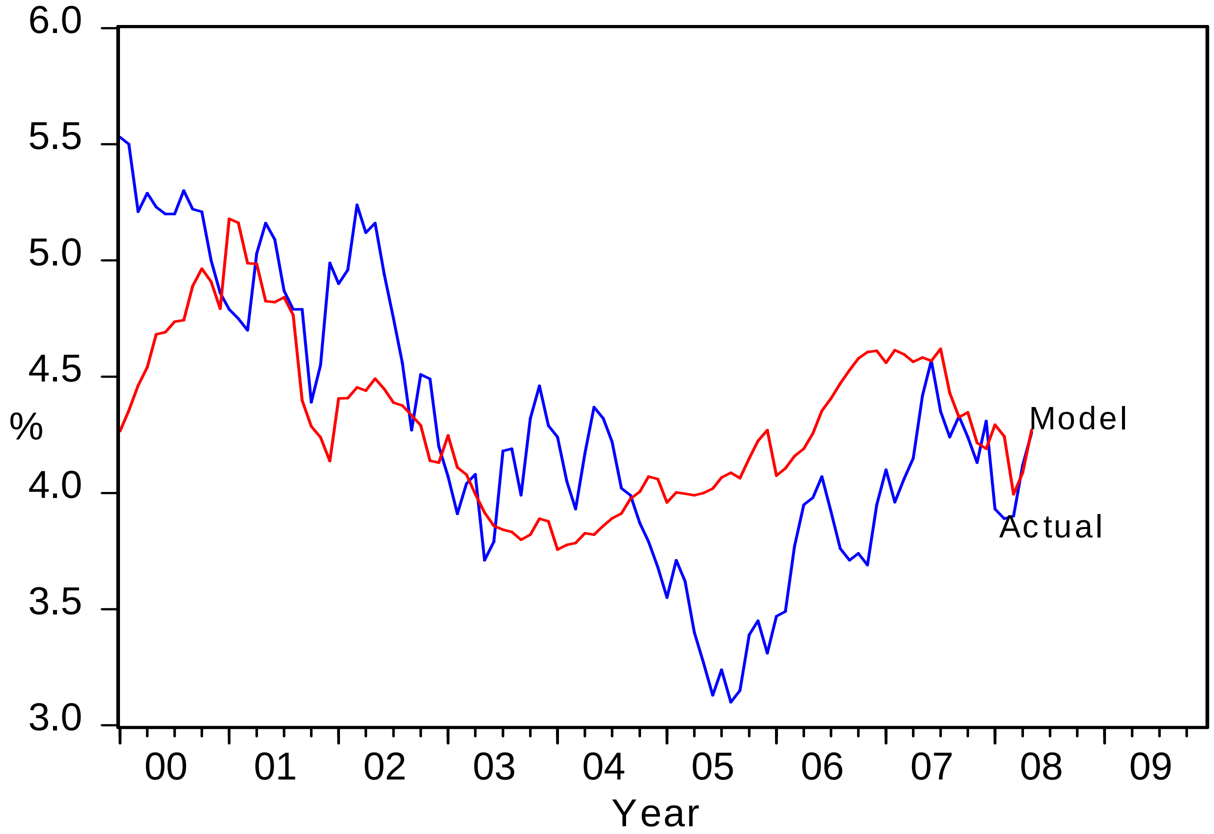
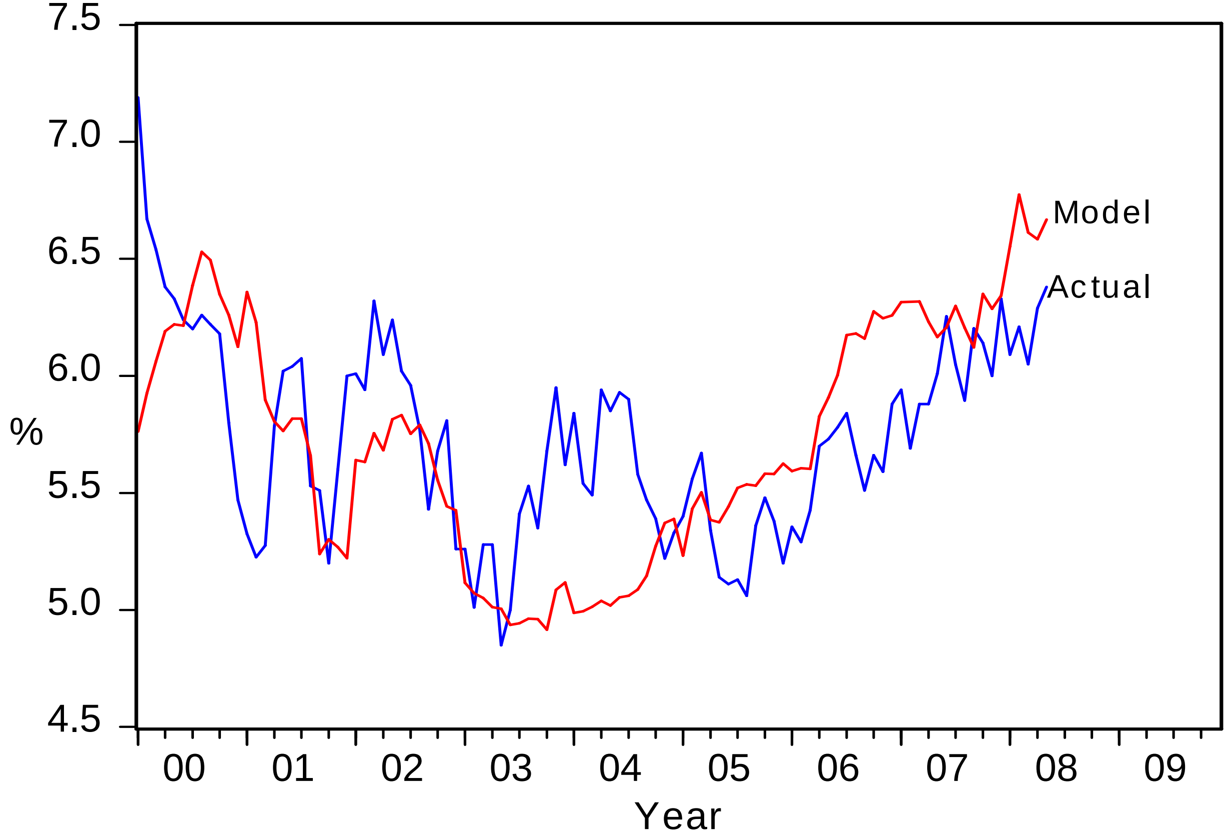
German Bund Yield Versus Appropriate Model Value – January 2000 to May 2008



The actual traded level of German Ten Year Bund yields on 21 May at 4.26% is almost identical to our model estimate of 4.27%.

Australian Ten Year Bond Yield Versus Appropriate Model Value – January 2000 to May 2008



At 6.38% on 21 May, Australian Ten Year bond yields are 29 basis points below appropriate yield of 6.67%.

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Clues to The Fed’s Monetary Policy

“New orders for equipment and software hesitated in the middle of 2000 and then fell sharply as firms re-evaluated their capital spending programs”.

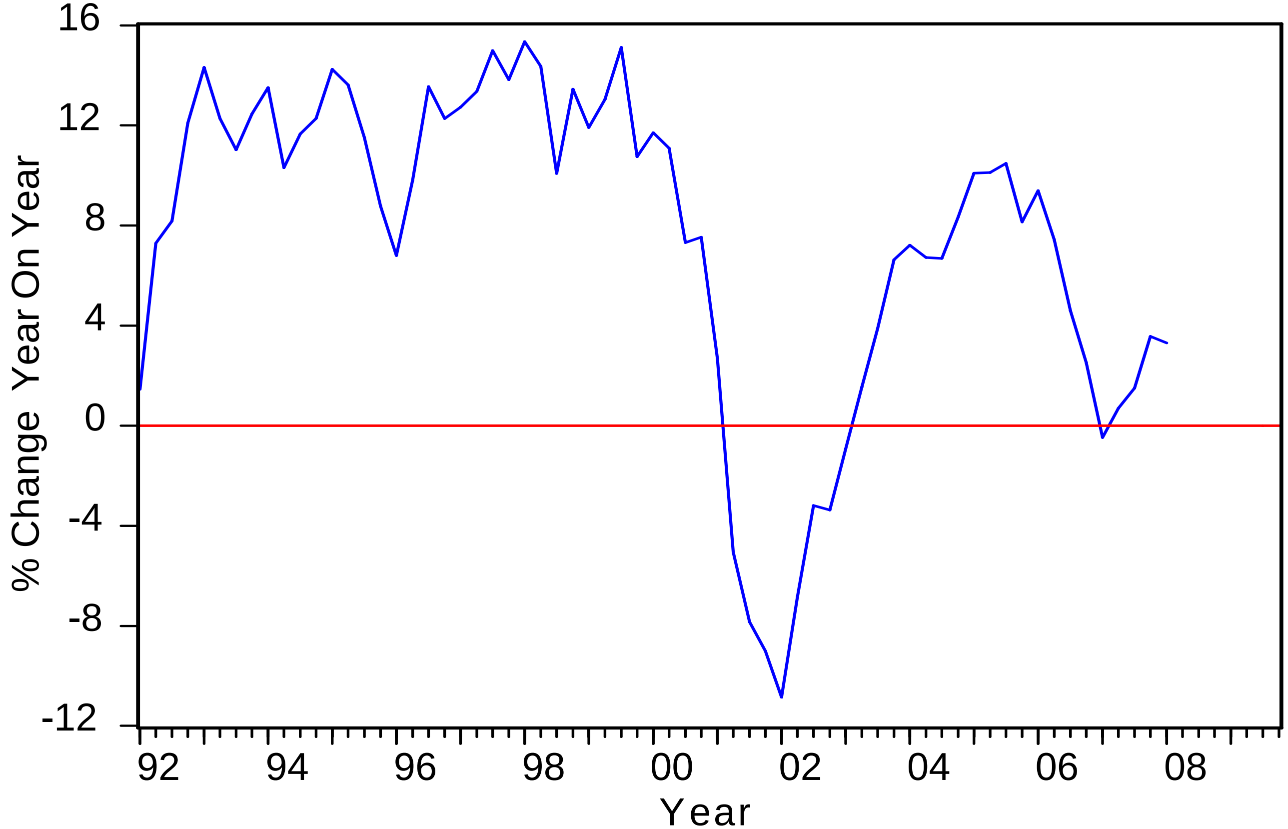
“These cutbacks in capital spending interacted with, and were re-enforced by, falling profits and equity prices”.

Alan Greenspan 24 January, repeated 27 February and 7 March 2002.

Our Approach:

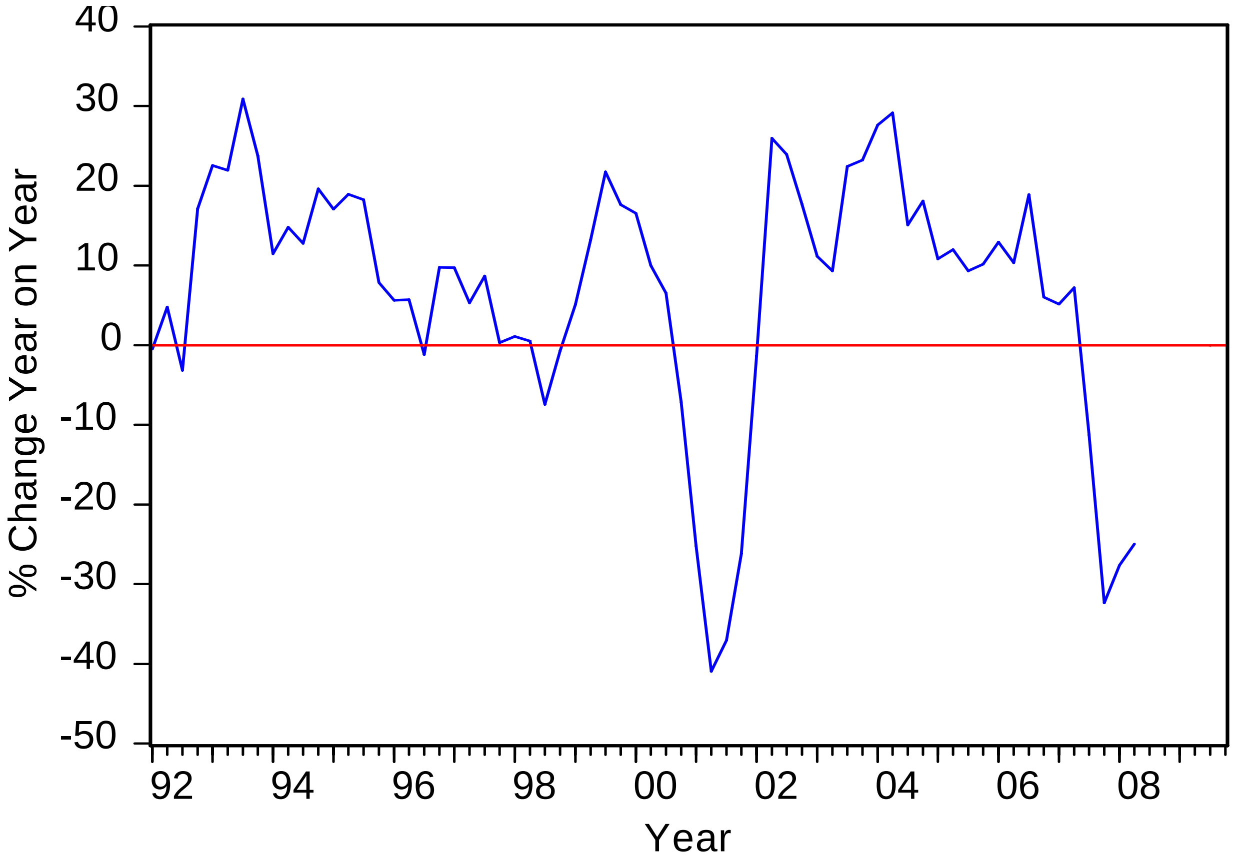
We investigate a model of the Real Fed Funds rate based on investment in equipment and software and operating earnings.

Real Investment In Equipment and Software Growth



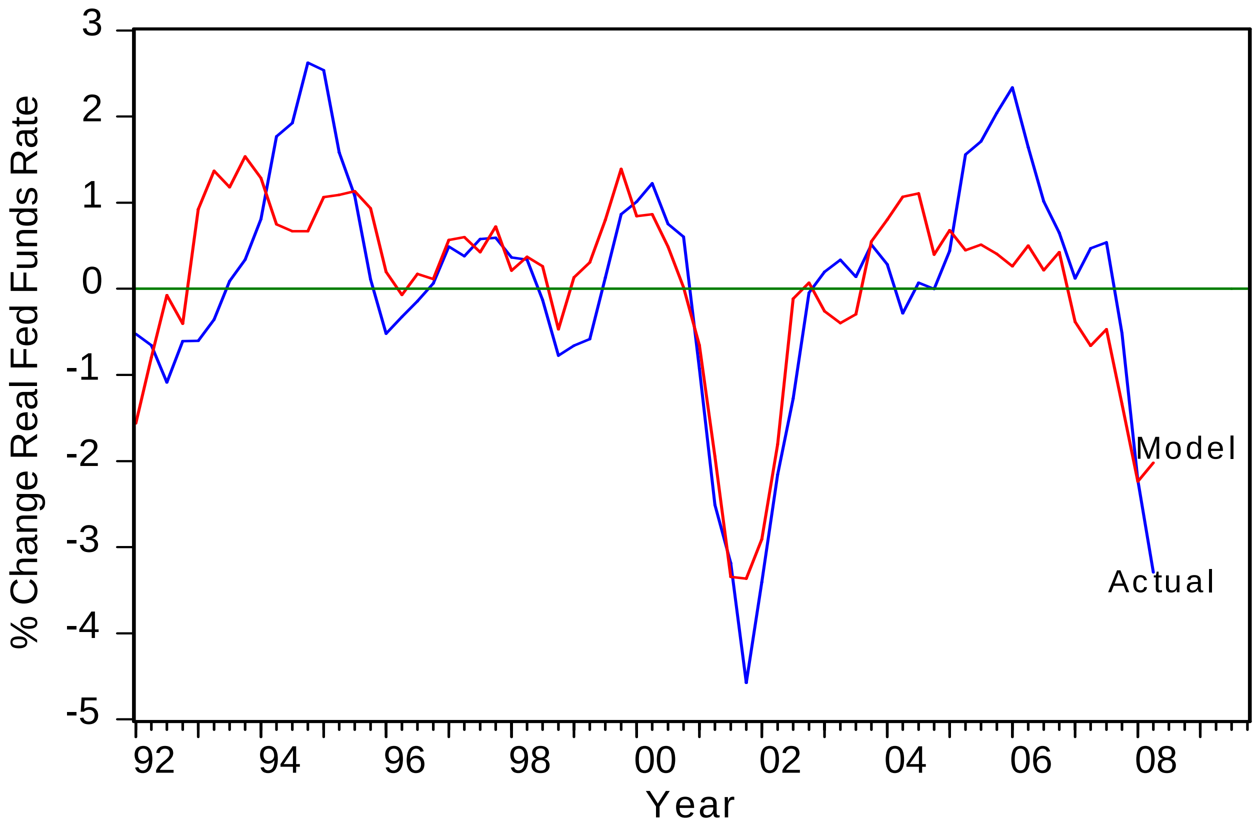
Real Tech Investment has only small positive growth.

Real Operating Earnings Per Share Growth



Real Operating Earnings Per Share has collapsed after the manner of the Recession of 2001.

A Model of Year on Year Changes In The Real Fed Funds Rate



The Fed is ahead of the curve for now. But falls in investment growth would lead to further cuts in Fed Funds.

Australian Short Rates

Our model suggests that neutral monetary policy for the Australian cash rate is 6.85%. However, monetary policy in previous tightening cycles has been 110 to 160 basis points higher than neutral.

This suggests the RBA is targeting a Bank Bill yield of 8.00% to 8.50%. The Bank Bill yield on 27 May of 7.74% may not be high enough.

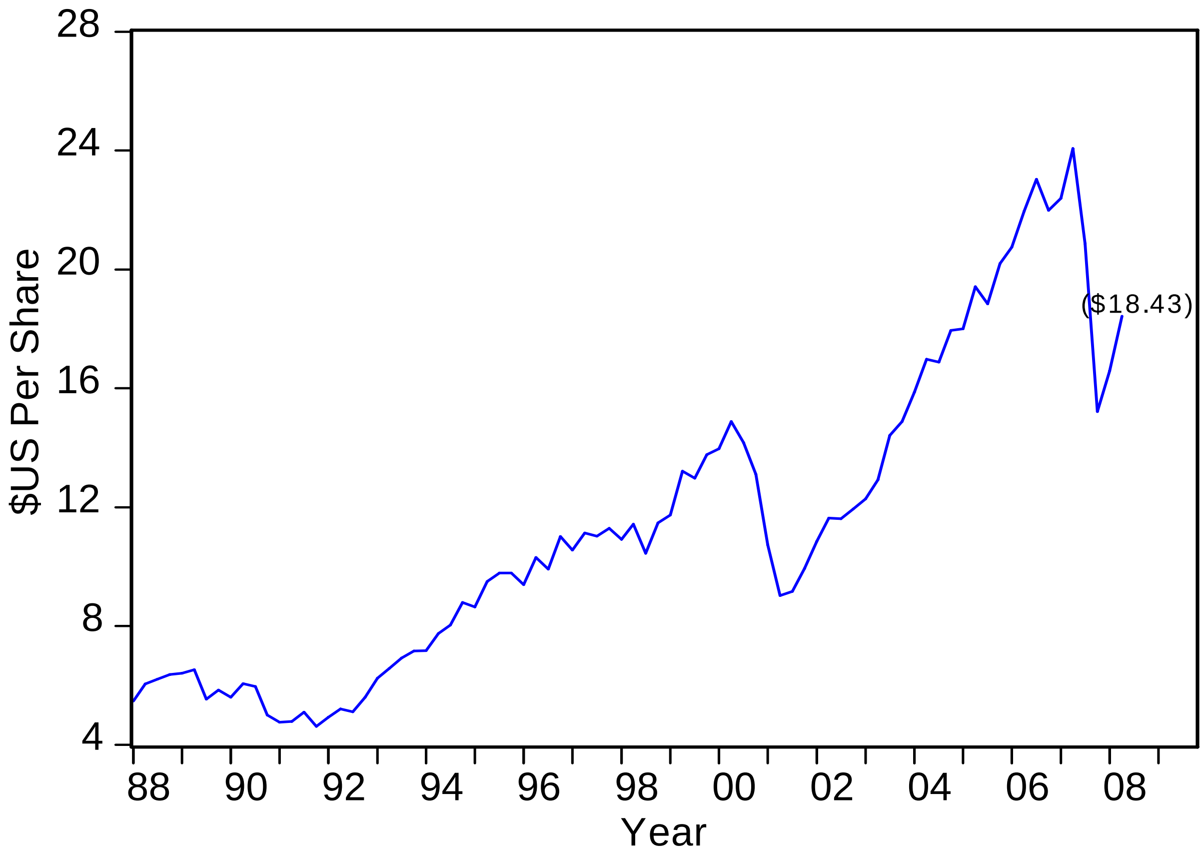
Euro Short Rates

Our model suggests the refinancing operations minimum bid rate (repo rate) has an equilibrium yield of 4.00%*.

This suggests the ECB will leave rates unchanged for now. However, further rises in inflation should move the ECG to tighten again.

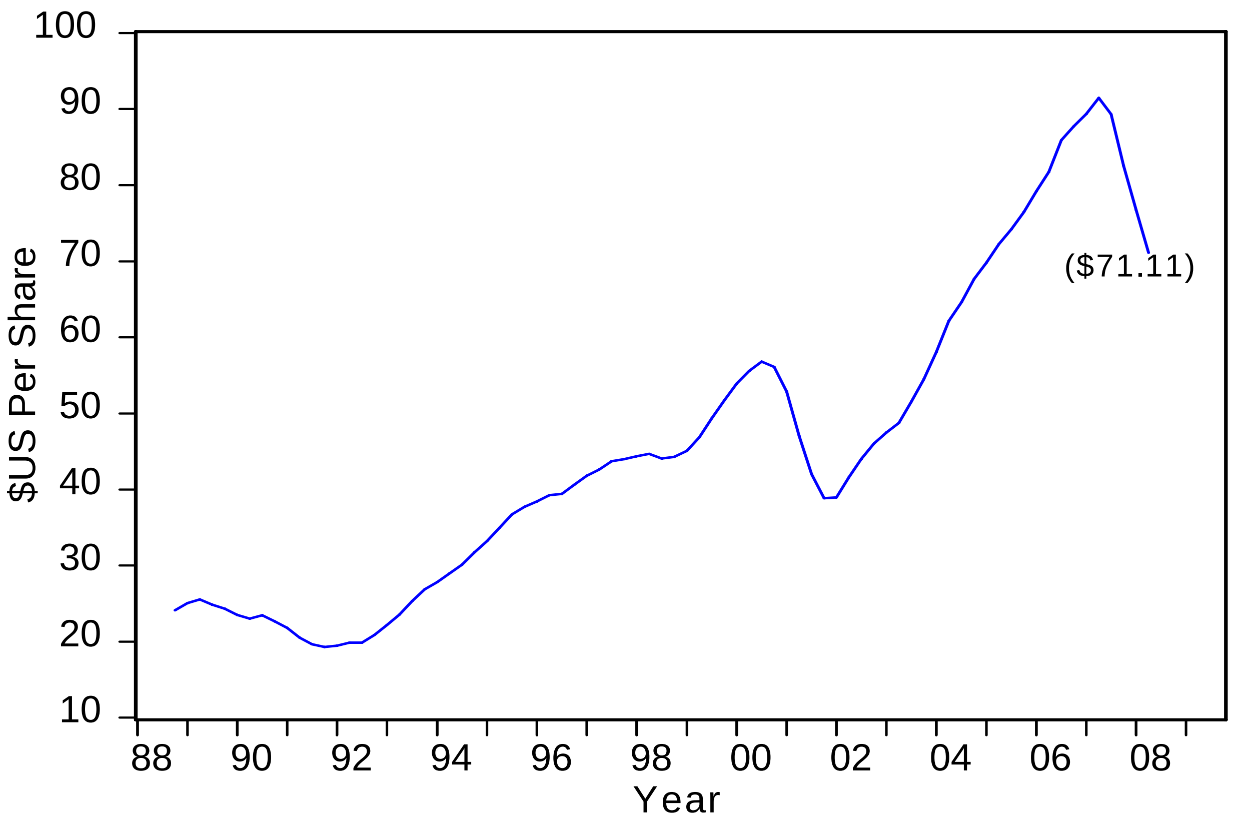
*** 3.99% model estimate**

S&P500 Quarterly Operating Earnings Per Share



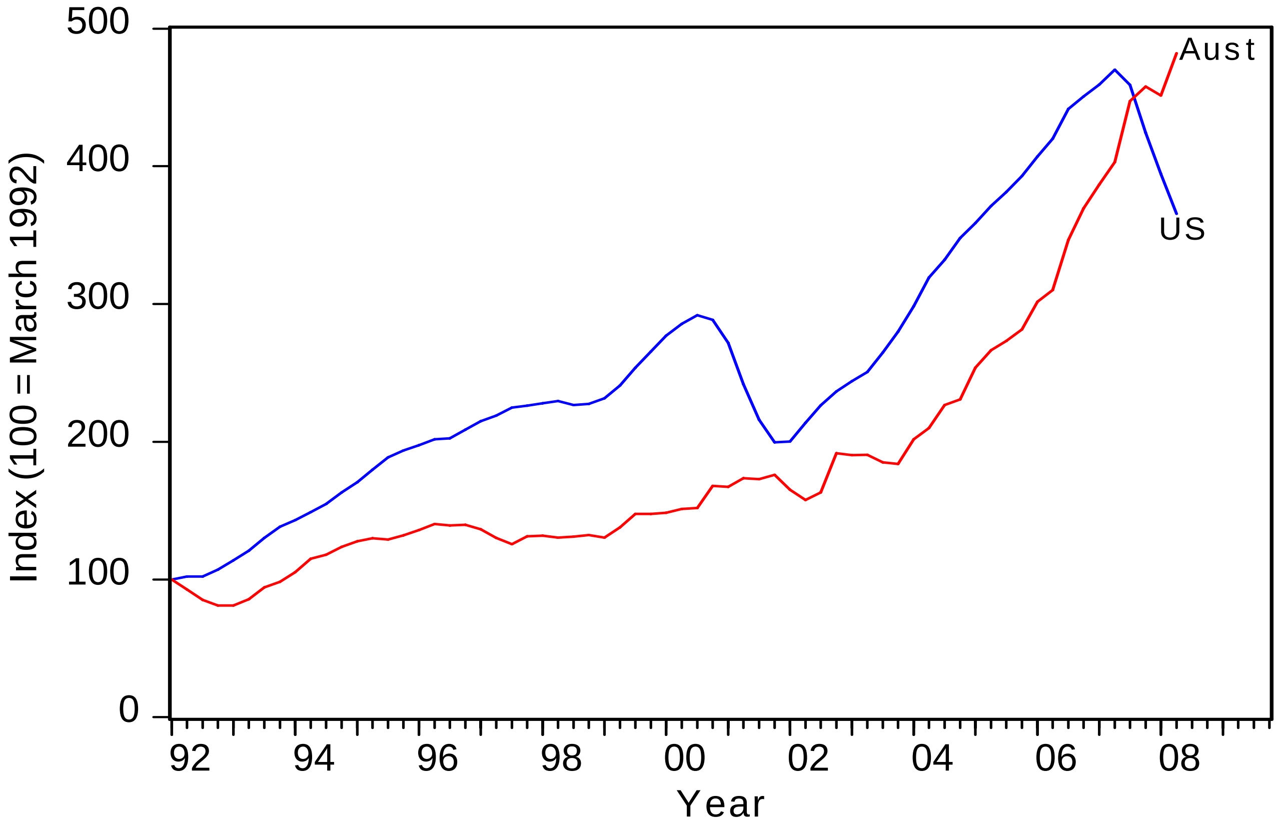
US Quarterly Operating Earnings Per Share may move to a (top down) estimate of $18.43 in the June quarter. This suggests operating earnings per share growth of -23.4% for the year to June.

S&P500 12 Month Rolling Operating Earnings Per Share



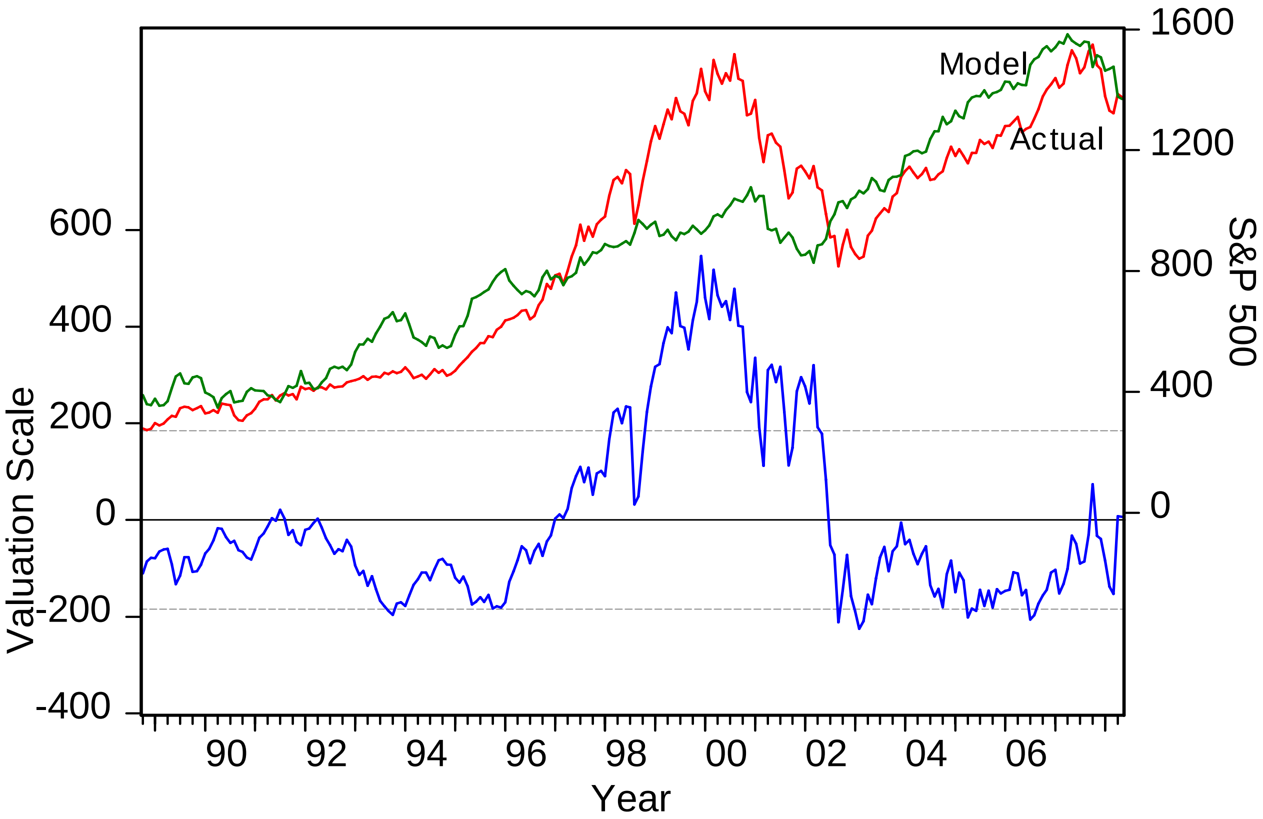
US 12 Month rolling Operating Earnings per share for the year to June may total $US71.11 per share ($US20.36 lower than the peak in June 2007).

Earnings Per Share US (S&P500) and Australia (ASX200) – 1992 to 2008



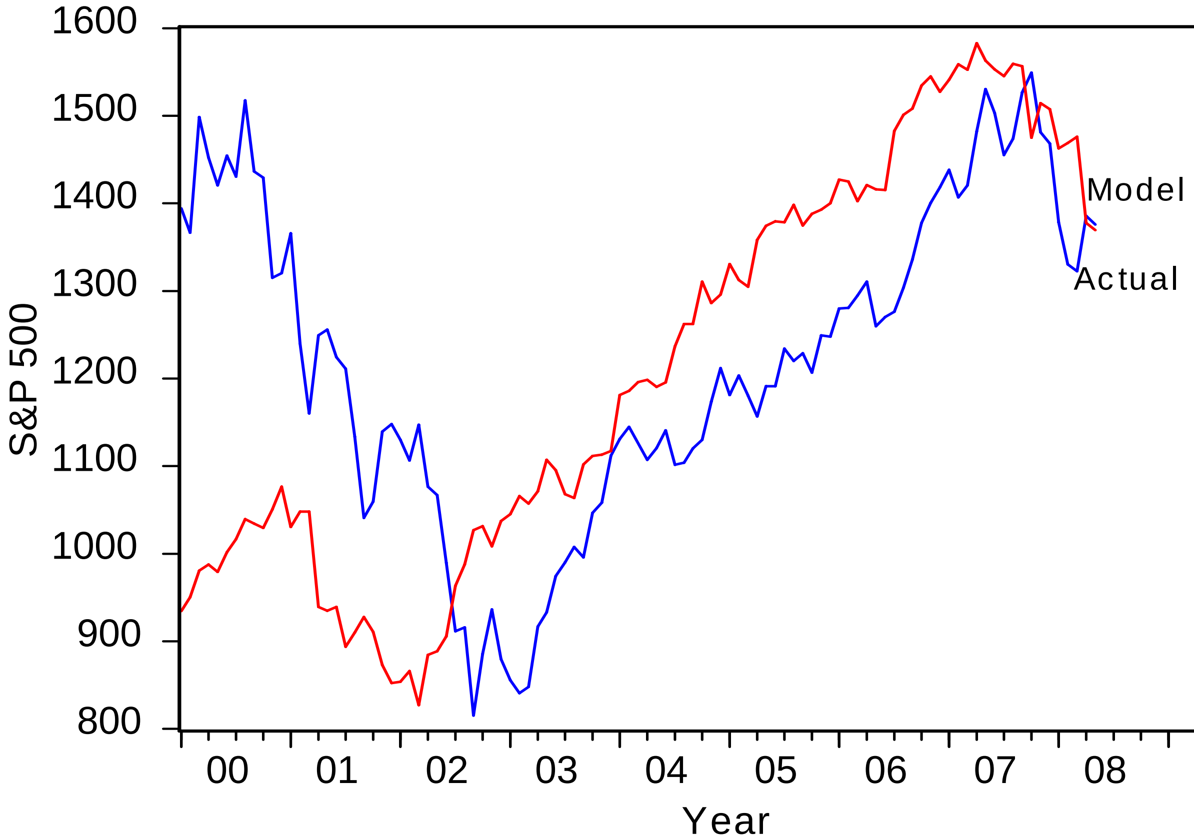
12 month operating earnings per share is down 22.25% in the US and up 22.3% in Australia.

Earnings Per Share and Bond Yield Model of the S&P500



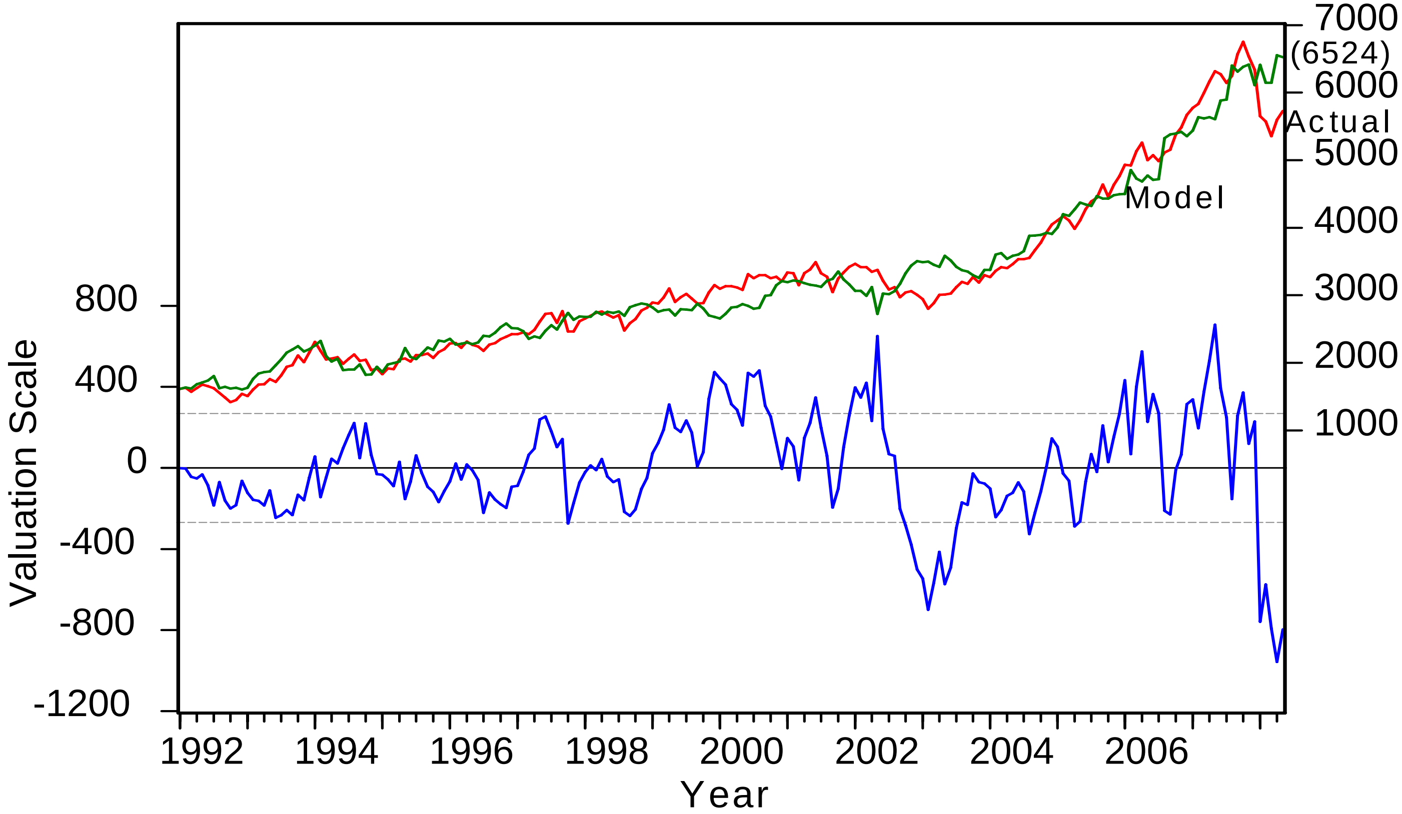
On the basis of Earnings Per Share and bond yield, fair value for the S&P500 on 24 May was 1,369 points (11,994 Dow Points) or 6 points below the traded value of 1375.

S&P500 Versus Appropriate Model Value – January 2000 to May 2008



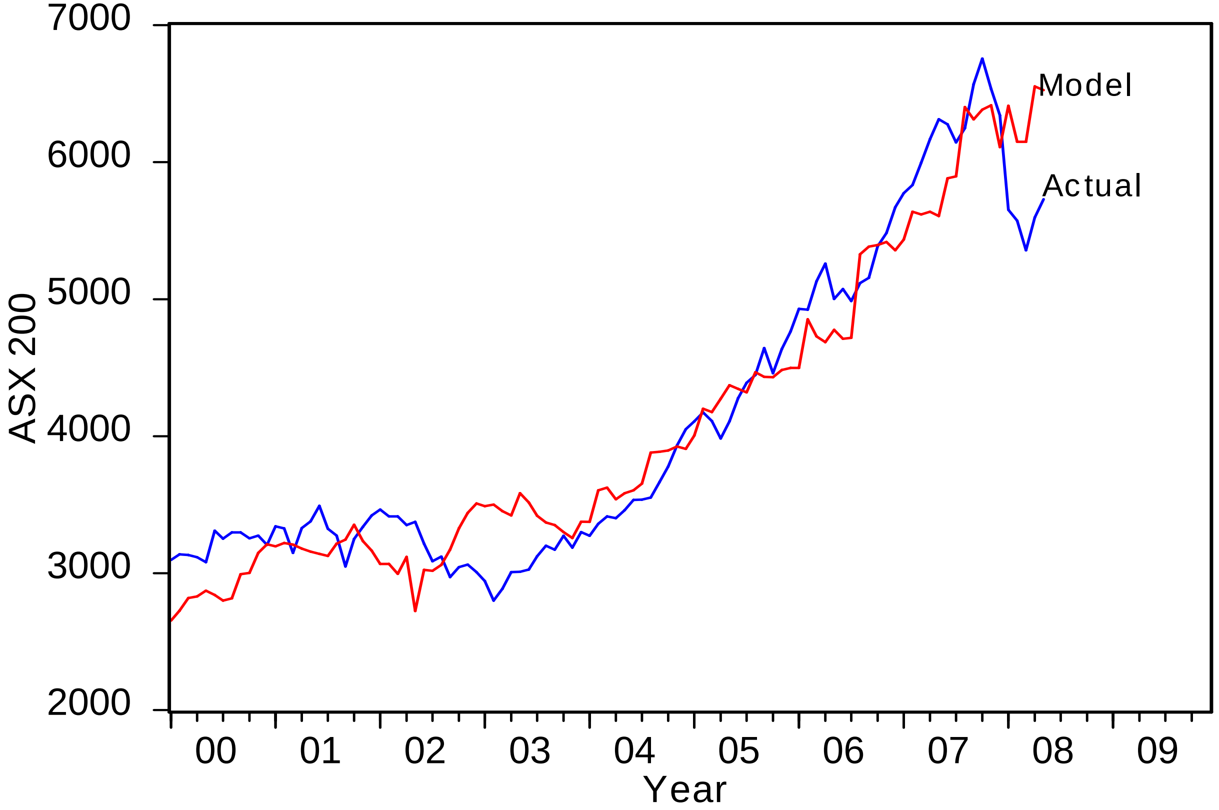
Falling earnings have collapsed the model value back to 1369. There can be little upward movement until earnings growth resumes.

Earnings and Bond Yield Model of the ASX 200



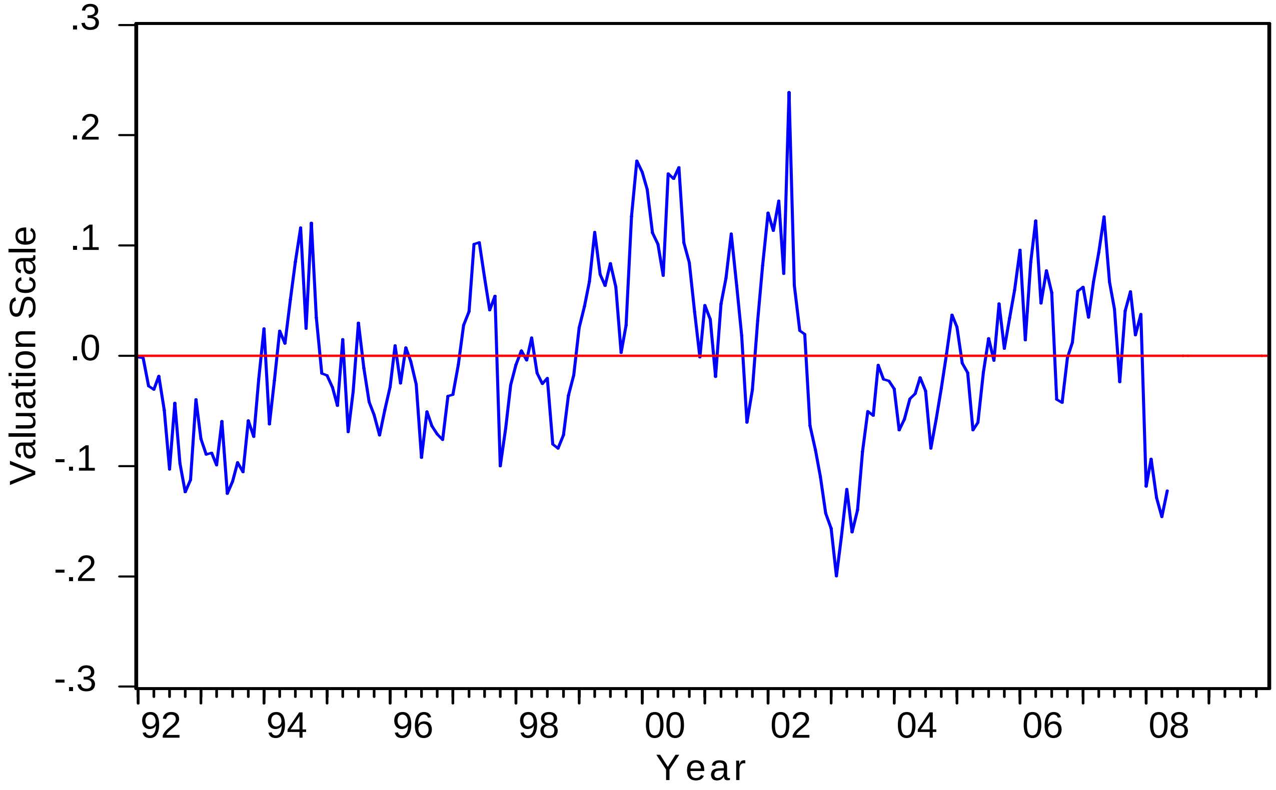
On 27 May, the ASX200 at 5727 points was 797 points below fair value of 6524 points.

ASX200 versus Appropriate Model Value
- January 2000 to May 2008



Our model explains 95.5% of monthly variation of the ASX200. The market is deeply undervalued. We expect it will rise towards fair value by December.

ASX200 Premium / Discount to Fair Value



On 27 May the ASX200 was at a discount of 12.22% to fair value. This compares to a discount of 12% during the first Gulf War in 1992, 7.5% during the bond crash of 1995, 9% during the Asian crisis of 1997, 7% during the Russian bond crisis of 1998 and 20% during the tech crash of 2003.

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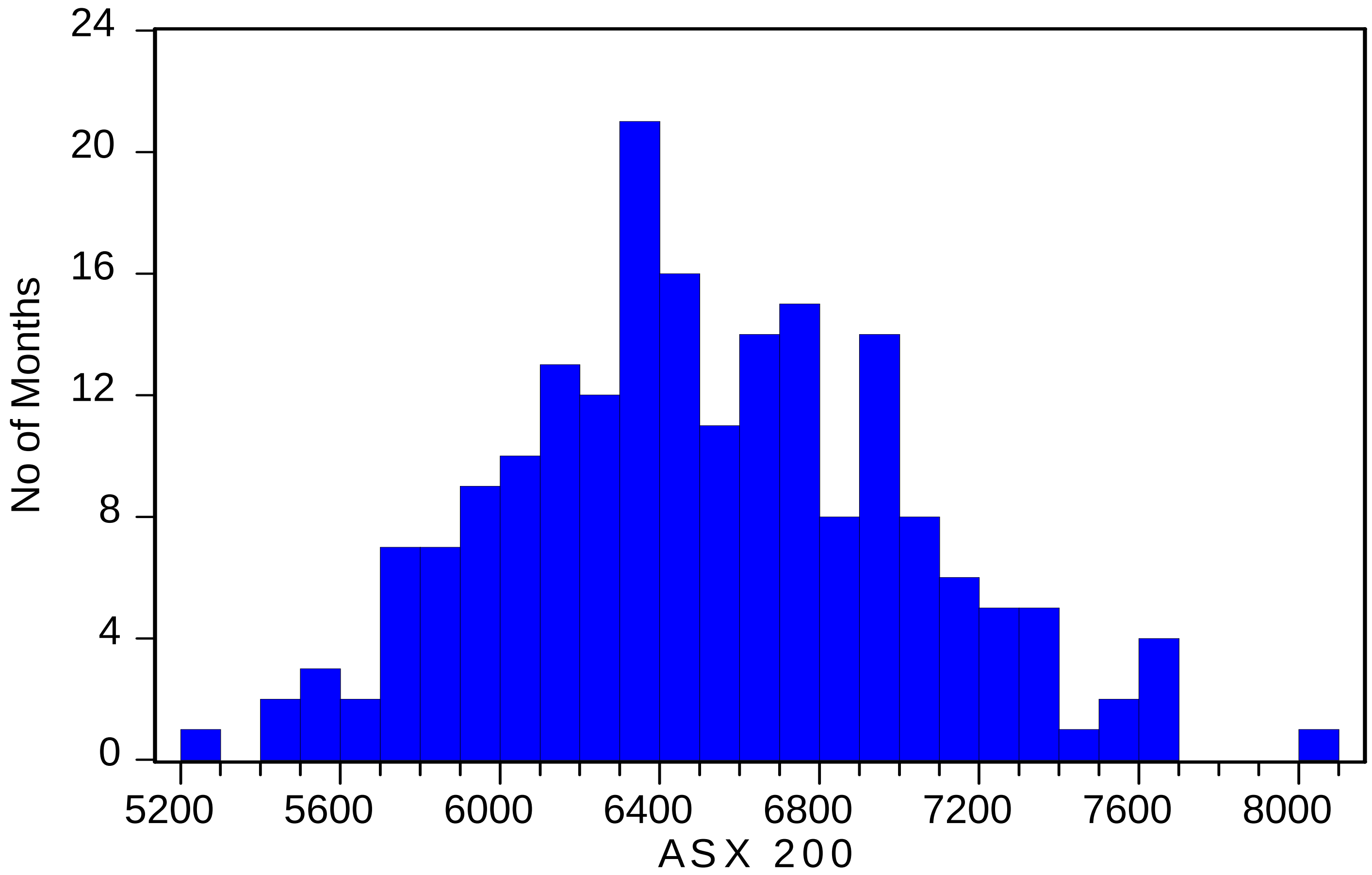
Distribution of ASX200 based on Fair Value of 6524.1



The lower limit of the distribution is 5221 points at a current fair value of 6524.1.

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