

SIM Wholesale Australian Fixed Interest Fund

Quarterly Investment Report March 2012

Fund Summary

Investment Objective: The objective of this Fund is to outperform (before ongoing fees) the UBSA Composite Bond Index (All Maturities) each year.

APIR Code: SUN0112AU

Fund Establishment: 31 May 2004

Management Costs: Up to 0.50% of the Fund's asset value

Market Review

The SIM Wholesale Australian Fixed Interest Fund outperformed its benchmark, the UBSA Composite Bond Index (All Maturities) in the March quarter. There was a relatively positive start to the year, with market sentiment improving although yields still remained fairly low. The three-year bond yield rose from 3.13% at the start of the year to 3.48% at the end of March, with 10-year yields up to 3.98% from 3.67%.

Domestic data remains mixed over the course of the quarter. The goods and services trade surplus was up from \$1.34 billion to \$1.71 billion due to a 2% rise in exports vs. a 1% rise in imports, beating market expectations. Building approvals remained weak despite a small rise in January. Private sector credit was up in both January and February and new home sales rose in February for the first time in three months. It is possibly the effect of the lower interest rates starting to filter through to credit growth and better demand for new housing. The ABS job vacancies series rose by 0.7% over the three months to February.

Data was released on capital expenditure for the fourth quarter of 2011 and it was down 0.3% quarter-on-quarter but there was a further extremely large rise in expected capex for 2012-2013. Businesses reported a 28.2% rise in estimated capex for 2012-2013 vs. the corresponding estimate for 2011-2012. This was almost entirely concentrated in the mining sector.

The Reserve Bank of Australia (RBA) maintained the cash rate at 4.25% in February, March and April as was widely expected by market commentators. The April statement indicated that output growth may be slightly weaker than the RBA had previously assumed, but it also "thought it prudent to see forthcoming key data on prices to reassess its outlook for inflation, before considering a further step to ease monetary policy". Clearly the RBA is waiting to see first quarter inflation data, which it gets later in April.

Market Outlook

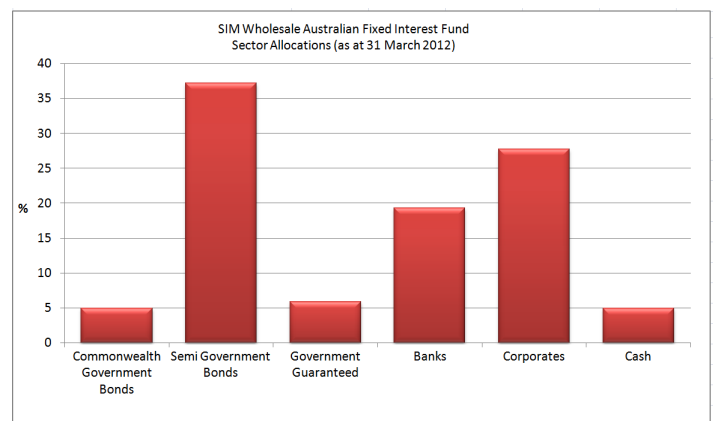
The bond market is still adjusting from its previously extreme expectations of rate cuts, but is troubled by the "risk on" / "risk off" movements in the financial markets. Commonwealth government securities (CGS) remain expensive and as one of the few remaining countries with an AAA rating from all three rating agencies, prices are being driven by flight to safety buying from foreign investors. Another factor affecting CGS is that US Treasury bond rates remain expensive as the US Federal Reserve continues its various programmes to keep long-term risk premiums low. Non-CGS paper remains cheap compared with government bonds.

The domestic economy is still being driven by a strong mining sector and strong expectations of future capital expenditure. The dollar remains absolutely strong which is having knock-on effects on the tradeable sectors and tourism, as well as magnifying fundamental changes in the economy that are affecting sectors such as retail. There is little the RBA can do to help individual sectors transform, unless we see a significant rise in unemployment leading them to slash rates to very low levels. In 2011, currency appreciation allowed the RBA to cut rates as inflation eased back to the middle of its target range. With the US economy looking stronger, the Australian dollar may start to weaken against the US dollar. If this happens, the role it has been playing in constraining inflation may start to unwind, which the RBA will have to take into consideration. Additionally, Australia's low productivity growth is likely to add to the RBA's concerns over the inflation outlook.

Our view is that despite the fall in inflation, Australia still has underlying structural inflation partly caused by our low productivity growth. This will play a factor in whether the RBA cuts rates and will prevent them from keeping rates too low. However, a continuing strong currency and concern over bank lending margins could see rates fall to 4.00% (or possibly 3.75%) in 2102.

Sector Allocations

This graph shows the effective sector allocation for the SIM Wholesale Australian Fixed Interest Fund.



Fund Performance^{**}

Period ending 31 March 2012	3 months %	6 months %	1 year %	2 years % p.a.	3 years % p.a.	5 years % p.a.
Total Return	1.76	3.33	9.35	8.24	6.91	6.87
Distribution Return	0.00	3.45	13.87	9.59	8.67	7.93
Growth Return	1.76	-0.12	-4.52	-1.35	-1.76	-1.06
UBSA Composite Bond Index (All Maturities)	0.78	2.74	10.00	8.41	6.48	7.26

^{**}All performance figures are calculated using hard close end of month exit prices and do not include any entry or exit fees or any taxation consequences and are net of nominal transaction and banking costs in any underlying funds invested in. The performance figures do allow for the historic ongoing fee. Income and distributions are assumed to be reinvested back into the Fund.

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Performance Graph

This graph compares the value of \$10,000 invested in the SIM Wholesale Australian Fixed Interest Fund since May 2004 against its benchmark.

