Greencape Wholesale High Conviction Fund

Fund report and commentary – 30 June 2008

Overview: The Greencape Wholesale High Conviction Fund (Fund), posted a return of 1.43% (after fees)* for the quarter compared with the S&P/ASX 200 Accumulation Index (benchmark), which returned -1.79%.

Performance

	3 months (%)	1 year (%)	3 years (%) p.a.	5 years (%) p.a.	Inception (%)
Greencape Wholesale High Conviction Fund	-0.69	-5.92	**-**	**-**	18.11
Growth return	-4.38	-11.32	-	-	7.91
Distribution return	3.69	5.40	-	-	10.20
S&P/ASX 200 Accumulation Index	-1.79	-13.40	-	-	6.12
Active return (net)	**1.10**	**7.49**	**-**	**-**	**11.99**

Returns are calculated after fees have been deducted, assuming reinvestment of distributions. No allowance is made for tax. Past performance is not a reliable indicator of future performance.

Investment objective

The Fund aims to provide capital growth over the long term through a highly concentrated portfolio of Australian shares, and provide returns above the benchmark, the S&P/ASX 200 Accumulation Index, over rolling three-year periods.

Investment manager

Greencape Capital Pty Ltd

Investment strategy

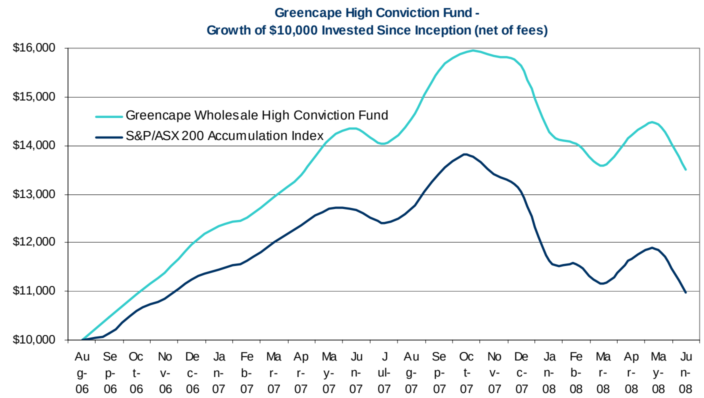
Greencape is an active, bottom-up stock picker. Whilst not targeting a specific investment style and investing in stocks displaying 'value' and 'growth' characteristics, Greencape's focus is on a company's qualitative attributes, which will generally lead to 'growth' oriented portfolios. This is an outcome of Greencape's bottom up process. As such, Greencape's investment style may be classified as 'growth at a reasonable price' (GARP).

Distribution frequency

Quarterly

Suggested minimum investment timeframe

At least five years



Asset allocation

	Current (%)	Range (%)
Securities	89	85 - 100
Cash	11	0 -15

Fund facts

	Greencape Wholesale High Conviction Fund
Inception date	11/09/2006
APIR code	HOW0035AU

Fees

	Greencape Wholesale High Conviction Fund
Entry fee	Nil
2006/07 ICR	0.90%
Management fee	0.90%p.a.
Performance fee	15% of the Fund's after management fee return above the Fund's benchmark.
Buy/sell spread	+0.30%/-0.30%

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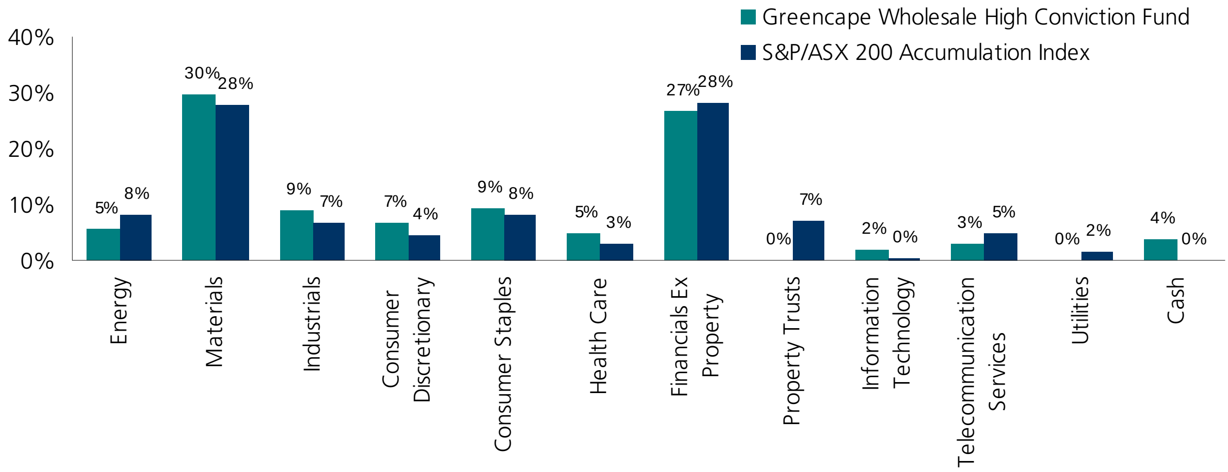
Sector exposures as at 31 May 2008



Market Review

For the June quarter the S&P/ASX 200 Accumulation Index fell 1.8%, capping off the 3rd third consecutive quarter of negative market returns and the largest financial year decline (13.4%) since 1982. The fall of 7.5% in the month of June was also the worst June performance in the Australian market since 1940, at the time when Germany was invading France!

The quarter and financial year performance varied significantly by sector with some of the largest moves shown below:

	June Quarter	FY08
Best performing sectors:		
Energy	34.0%	35.0%
Materials	11.9%	18.1%
Worst performing sectors:		
Property Trusts	- 17.2%	- 40.3%
Consumer Discretionary	- 22.5%	- 43.2%
Industrials	- 16.0%	- 36.5%
Financials (ex Property Trusts)	- 10.1%	- 33.5%
Utilities	- 5.7%	- 31.6%

As the table above shows Energy stocks dominated the quarter with the oil price rising from US $102 (WTI) to US $140 over the period.

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Materials also posted a very strong quarter led by Fortescue Metals up 83% and BHP up 22%.

Banks held up for the first part of the quarter but then declined 18% from mid May to the end of the quarter.

Company Visits and Observations

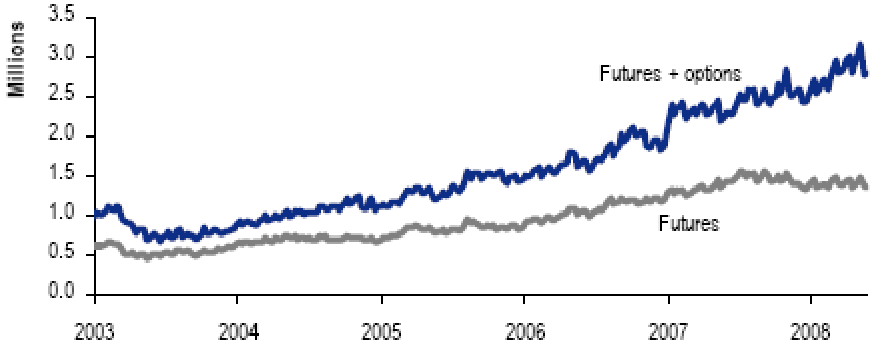
"Observations are for questioning before belief"

Arnold Wood CEO, Martingale Asset Management

- We witnessed a number of companies provide profit warnings due to the sharp rise in oil prices during the quarter. Imdex (a mining product supplier) and Transfield Services (commercial services) are examples of companies that face time delays before they are able to reprice contracts to fully pass on higher fuel prices, and thus their final quarter earnings for FY08 have been negatively impacted.

- In May, testimony was presented by a hedge fund manager to the US Department of Homeland Security which drew attention to the level of speculator demand in commodities futures markets. The submission highlights the recent trend for institutional investors (e.g. pension funds) to allocate a portion of their portfolios to commodities futures. These types of investors are now the largest players in some markets compared to 5 years ago when they were only a small fraction of volumes traded. The conclusion of the report is that speculators are the main cause of high commodity prices and it recommends the US Congress act to prohibit such speculation. Given the impact oil prices are having on consumers and businesses around the world, and the pressure being placed on governments to act it will be interesting to see if any action is taken, and what impact may follow on commodity prices. Below is an indication of growth in futures/options positions in the oil market.

Figure 10: Open interest in WTI – no. of contracts (1 contract = 1,000 barrels)



Source: Bloomberg

- In May we visited companies in Hong Kong, the US and Canada. The disparity between the outlook of managers in each country was profound. US retailers were bearish on their near term outlook and broadly expected consumer spending to weaken further during 2008. In contrast, retailers in Hong Kong were not concerned with demand slowdowns in their regional market, and were focused on continued store rollouts and margin expansion, however rising input cost inflation from China was a common theme.

- We met with a diverse range of companies in the US and note the following observations:
  - Consolidation in building products has allowed companies to date to increase prices despite the housing market being in its 10th consecutive quarter of a downturn
  - US infrastructure is generally in poor shape (airport capacity, roads, etc.)
  - Competition by share trading platforms is fierce
  - Large retailers are micro-managing their cost base to extract savings wherever possible (e.g. collecting rubbish every 10 days vs. every week!)
  - The trend towards facilities management outsourcing continues
  - Any medical goods and services suppliers that rely on Medicaid reimbursement are likely to face continued pressure to reduce their prices

"There's no reason why McDonalds should be forced to buy its potatoes through Coles"

Stephen Zilioli, Liquidnet, re ASX's monopoly of equities trading in Australia

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- In May we attended the Berkshire Hathaway AGM in Omaha, Nebraska USA along with 31,000 other shareholders. Warren Buffet and Charlie Munger held a question and answer session which we found extremely interesting and insightful, particularly given the volatile market gyrations that had occurred in global credit markets in early 2008. Below are a few notable quotes from Warren and Charlie:
  - *"We ignore 99% of what we see"*
  - *"You need to be happy with your purchase as if the market was going to be closed for the next 2 to 3 years"*
  - *"Students at business schools learn complex option pricing formulas, which have nothing to do with investment success. Investors really only need to know two things: 1 – How to value a business; and 2 – How to think about stock market fluctuations"*
  - *"Never trade reputation for money"*
  - *"We would be very happy with a 10% p.a. pre-tax return over the long term and we would probably settle for a little less"*
  - *"We've just stuck with what we understood and done for years, its just the nature of compound interest"*
  - *"We prefer businesses that drown in cash"*
  - *"You want to buy companies so good that even an idiot could run it, because sooner or later one will!"*
  - *"Investment banks are too big to be allowed to fail. It's a crazy situation"*
  - *"In the drug market you have to prove a drug works before you can sell it. On Wall Street some start believing in the tooth fairy, then others see people making money in tooth fairies and ask why we don't believe in it too?"*

- US house prices have declined 18% since their peak in July 2006 (S&P Case Shiller Index). The charts below show the magnitude and length of past periods of real house price rises and falls. Of particular interest is the relative size and length of the most recent housing boom.

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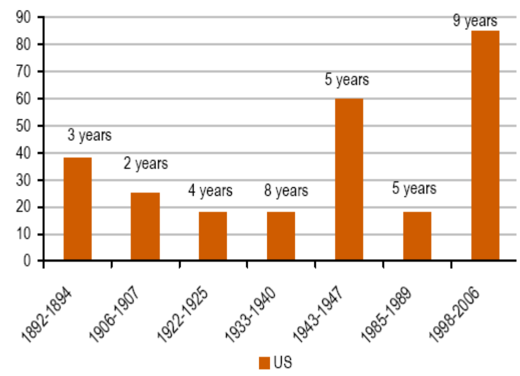
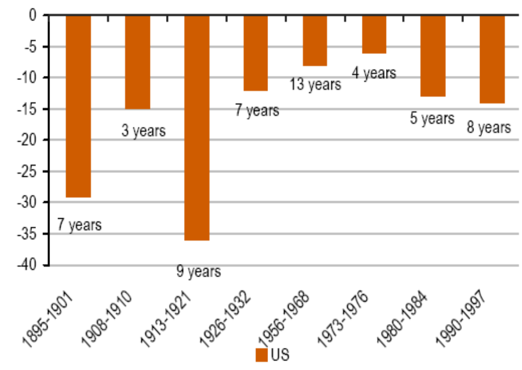
Fund report and commentary – 30 June 2008

Chart 13: US real house price feast.....



Source: UBS

Chart 15: US real house price famine



Source: UBS

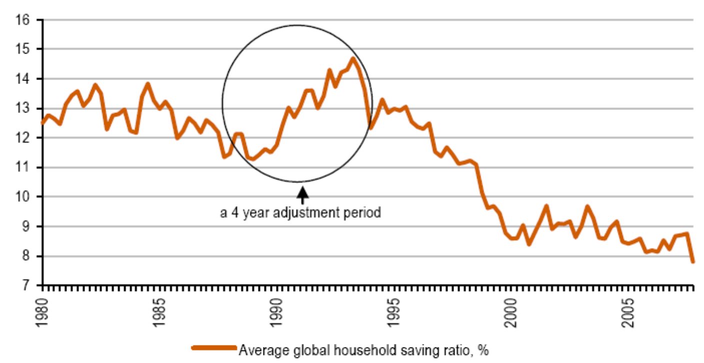
Fund outlook

The global economy has benefited from a decline in savings rates over the past decade. With inflation expectations rising, higher cost of debt and reduced debt availability, we expect households and corporations have begun a period of de-leveraging which will be negative for global GDP growth for some time.

"Historically, societies that seek high levels of instant gratification and are willing to borrow against future incomes to achieve it have more often than not suffered inflation and stagnation."

Alan Greenspan, The Age of Turbulence 2007

Chart 18: Global household saving rates are at record lows



Source: UBS calculations. Based on data for the OECD and several major developing economies (including China, India, Russia and Brazil)

"The de-leveraging process is one that is measured in quarters and years."

George Magnus Senior Economic Advisor UBS, June 2008

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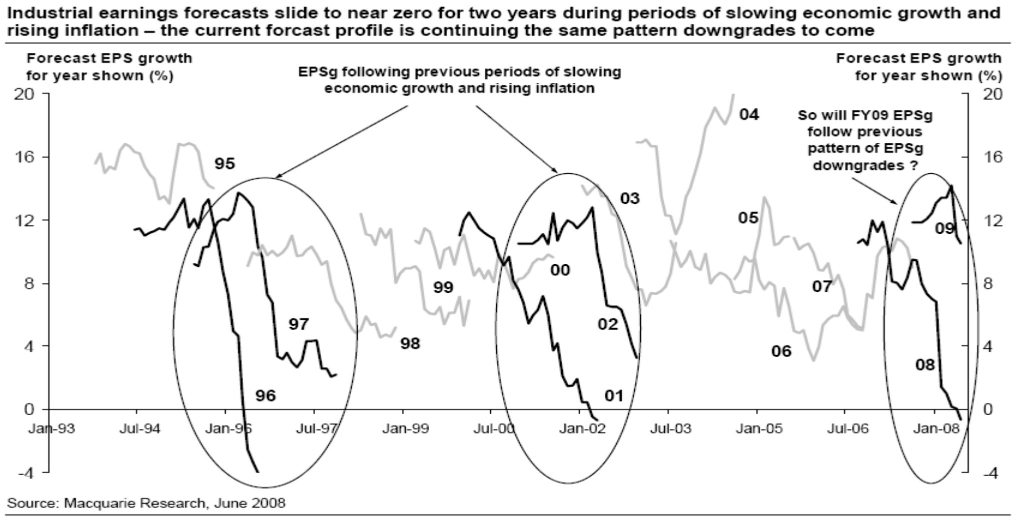
At the time of writing Macquarie Bank brokerage were forecasting 31% EPS growth for FY09, with Industrial companies' earnings expected to grow 10%. With GDP growth expected to slow these forecasts appear optimistic and in our view are likely to be revised downwards over the coming months. The chart below shows how EPS forecasts have been revised over time in the past. We note that in previous earnings downgrade cycles the bulk of the downward revision has occurred within the forecast year, implying that analysts remain optimistic until shown evidence to the contrary!

> ***"Wall Street traders make an annual bonus and get an annual review based on risks that don't show up on an annual basis. You have all the incentive in the world to take these risks."***
>
> **Nassim Taleb, AFR 30/01/08**



We continue to use this period of market uncertainty to concentrate the portfolio towards quality companies at attractive prices. We expect these businesses to be better placed to weather reductions in demand and protect margins in a tough operating environment. Such companies are expected to be the first to rebound as markets stabilise and confidence begins to return.

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