

Dear Members,

Investors have had an endless fascination with the stock market ever since public trading first began over 300 hundred years ago. This is unlikely to ever change, and fortunes will continue to be made and lost like the rhythms of the tide. Anything can happen in the stock market, and what is perceived as concrete and permanent today, is often gone with the wind tomorrow.

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There are few absolute laws of the stock market that have held true over the centuries. Sir Isaac Newton, the famous English scientist and perhaps one of the most intelligent individuals to ever walk the earth, had serious issues understanding the market. In the early 1700s, Sir Isaac became enamoured with the soaring prices of the South Sea bubble and bet heavily with his fortune. After the bubble imploded, prices collapsed and Sir Isaac lost much of his wealth. Even more distressing was the fact that apart from being a famous scientist, Sir Isaac was also the Chief Executive of the Royal Mint - you would have thought he might have known better.

Perhaps US Federal Reserve Chairman, Alan Greenspan, would do well to research this period of history, because the hard won lessons of Sir Isaac over 300 hundred years ago seem to have been forgotten today. Since Fat Prophets inception, we have strived to not only understand the past, but to apply these lessons to our value orientated investment processes as diligently as possible. The outcome has not always been "fat profits" for our Members, but it is fair to say that, on balance, more profits have been won than losses incurred.

We recently marked our fourth anniversary as an independent research provider, during which time we have witnessed the market's extremes. This year however has been a relatively smooth ride for most investors with the All Ordinaries Index making record highs. Nearly all sectors of the market have achieved out performance, and many investors are sitting on profits.

With the property market coming off the boil and residential real estate no longer delivering easy gains, capital has flowed back into equities. However, accompanying the rise in the market has been an increase in risk in our view. Investors should proceed with caution, and perhaps now is a time to consider locking in some profits - as we have recommended doing so in recent months. An old saying comes to mind, first coined by the famous Wall Street investor Bernard Baruch more than 80 years ago, that "no one ever went broke by taking a profit early".

At the start of the year, we made five key predictions with respect to Australian and US equities, gold, global interest rates, financial stocks and currencies. We outlined a sixth prediction during the first quarter concerning the oil price. While not all our targets were met, we nevertheless foresaw the general trend of the global economic environment.

The call that was widest of the mark related to the Dow Jones and, to a lesser extent, the All Ordinaries. We continue to be amazed at the resilience of US equity markets, which maintained a firm tone throughout the year despite the excessive valuations. However with the S&P500 continuing to yield less than 2 percent, a major correction in 2005 is probable in our opinion.

Our expectation for a pullback in the All Ordinaries was also incorrect, although the view that local stocks would outperform most foreign indices proved more accurate. The Australian stock market was among the best performing in the OECD, with the All Ordinaries rising by close to 20 percent. A correction now seems likely in the first half of 2005 in our opinion.

"As evidenced by the 2004 report card, Members on balance have been very content with our performance with a 'B' being the average grade awarded."

Gold defied gravity throughout much of the year and seems destined to finish 2004 near a sixteen year high. Many analysts were surprised at the strength of the precious metal, which benefited from a falling US dollar, rising investment demand, and geopolitical tensions in the Middle East. In January we predicted the gold price would reach US\$500 an ounce by the end of the year. While gold did not quite reach these highs, we have nevertheless been encouraged by the strength in the metal. Since 2001, we have maintained a bullish outlook for gold. This has been the correct view with bullion and gold stocks rising within a strong bull market. We believe further gains will materialise next year, although the prospects of a healthy correction in the near term are high.

Rising interest rates around the world also came to pass, and in Australia this continued to have a cooling effect on the housing market. Short term interest rates in the United States more than doubled from 1 to 2.25 percent, and the bond market deteriorated in the fourth quarter, with yields also increasing at the long end of the curve. China raised rates for the first time since 1995 to cool the rapidly expanding economy. Canada and the UK also raised rates.

Despite upward pressure on interest rates, stocks within the financial sector held up much better than we anticipated. For some time our view has been that Australian bank shares would come under pressure as earnings growth slowed. Although this has yet to transpire in any meaningful way, we believe that financial stocks are still best avoided in 2005.

On the currency front we fared well. The Australian dollar rose to a seven year high of 80 cents, which was the level predicted back in January. The Euro also strengthened and came within a whisker of our projected level of Euro1.35 against the US dollar. The greenback continued to plummet like a lead balloon, and surprised most analysts on the downside. More turbulence seems probable in the year ahead.

Oil surprised the consensus when prices traded above US\$50 for the first time in history. Instability in the Middle East, soaring consumption in Asia - particularly in China - were the most apparent catalysts for the rise. Earlier this year we forecast that oil would trade well beyond US\$40 a barrel. At the time, this prediction

encountered widespread scepticism. However as history has repeatedly demonstrated, markets often pay little attention to the consensus outlook.

With respect to the Fat Prophets Portfolio, 11 out of the 13 stocks sold during the year yielded profits on the originally recommended buy price.

Company	Return	Buy	Issue	Sell	Issue
Wadepac (WDP)	#117.3%	\$1.30	FAT96	\$2.70	FAT206
Macarthur Coal (MCC)	#195.8%	\$1.25	FAT98	\$3.58 (half)	FAT202
Caltex (CTX)	#320.5%	\$2.15	FAT31	\$8.72 (half)	FAT198
Deutsche Ind. (DIT)	#72%	\$1.43	FAT23	\$1.92	FAT192
Emperor (EMP)	143.2%	\$0.37	FAT51	\$0.90 (half)	FAT189
Smorgon (SSX)	#-5.8%	\$1.29	FAT23	\$1.07	FAT187
Sims Group (SMS)	#117.7%	\$5.32	FAT56	\$10.42	FAT183
Nufarm (NUF)	#74.6%	\$3.62	FAT102	\$5.93 (half)	FAT182
MYOB (MYO)	#130.4%	\$0.60	FAT53	\$1.35 (half)	FAT181
Qantas (QAN)	#4.8%	\$3.75	FAT14	\$3.31	FAT180
Promina (PMN)	#108.5%	\$1.70	FAT127	\$3.42	FAT179
Caltex (CTX)	#282.8%	\$2.15	FAT31	\$8.05 (half)	FAT177
Palm Springs (PSG)	-34.2%	\$0.395	FAT21	\$0.26	FAT172

Denotes: # dividend included; (half) sold half

Recommendations that were made during 2004 (but not yet sold) also produced a positive result. Of the 48 buy recommendations, 33 are currently in profit. A number of stocks were recommended more than once, and thus some stocks have more than one entry on the table below. The majority of stocks presently showing a loss are in the "high risk" category, where greater volatility is expected. This highlights the importance of maintaining a well balanced and diversified portfolio.

Company	Return	Buy	Issue	Closing Price 21 December
Austal (ASB)	101%	\$0.98	FAT169	\$1.97
Oil Search (OSH)	68.5%	\$1.08	FAT170	\$1.82
Indophil Resources	65.4%	\$0.26	FAT185	\$0.43

(IRN)				
Lion Selection	60%	\$1.35	FAT179	\$2.16
(LSG)				
Tower	56.5%	\$1.24	FAT168	\$1.94
(TWR)				
Gallery Gold	55.6%	\$0.27	FAT186	\$0.42
(GN)				
Gallery Gold	55.6%	\$0.27	FAT175	\$0.42
(GN)				
Gallery Gold	55.6%	\$0.27	FAT173	\$0.42
(GN)				
Oil Search	49.2%	\$1.22	FAT178	\$1.82
(OSH)				
Indophil Resources	38.7%	\$0.31	FAT203	\$0.43
(IRN)				
Oil Search	35.8%	\$1.34	FAT191	\$1.82
(OSH)				
Fosters Group	34.3%	\$4.37	FAT171	\$5.87
(FGL)				
Mayne Group	33.2%	\$3.25	FAT184	\$4.33
(MAY)				
Mayne Group	32.4%	\$3.27	FAT170	\$4.33
(MAY)				
Austar	30%	\$0.70	FAT182	\$0.91
(AUN)				
Southcorp	30%	\$2.90	FAT169	\$3.77
(SRP)				
Burns Philp	29.2%	\$0.65	FAT177	\$0.84
(BPC)				
Pacific Hydro	28.4%	\$3.10	FAT195	\$3.98
(PHY)				
Fosters Group	27.6%	\$4.60	FAT195	\$5.87
(FGL)				
Gallery Gold	23.5%	\$0.34	FAT200	\$0.42
(GN)				
Village Roadshow	22.9%	\$1.70	FAT166	\$2.09
(VRL)				
Burns Philp	21.7%	\$0.69	FAT185	\$0.84
(BPC)				
Lihir Gold	21.6%	\$0.97	FAT182	\$1.18
(LHG)				
Burns Philp	16.7%	\$0.72	FAT190	\$0.84
(BPC)				
Southcorp	16%	\$3.25	FAT194	\$3.77
(SRP)				

Pacific Hydro (PHY)	13.7%	\$3.50	FAT206	\$3.98
Hutchison (HTA)	9.4%	\$0.32	FAT200	\$0.35
Austar (AUN)	8.9%	\$0.90	FAT187	\$0.98
Gallery Gold (GGN)	5%	\$0.40	FAT209	\$0.42
Village Roadshow (VRL)	4.5%	\$2.00	FAT208	\$2.09
Paperlinx (PPX)	3.6%	\$4.72	FAT174	\$4.89
Newmont Mining (NEM)	3.2%	\$5.70	FAT185	\$5.88
Paperlinx (PPX)	1.5%	\$4.82	FAT186	\$4.89
IWL (IWL)	-1.9%	\$2.16	FAT202	\$2.12
AuSelect (AUS)	-2%	\$1.00	FAT174	\$0.98
Village Roadshow (VRL)	-2.8%	\$2.15	FAT195	\$2.09
OceanaGold (OGD)	-3.5%	\$0.85	FAT177	\$0.82
Westonia Mines (WEZ)	-4%	\$0.25	FAT201	\$0.24
Lihir Gold (LHG)	-6.3%	\$1.26	FAT202	\$1.18
Lihir Gold (LHG)	-6.3%	\$1.26	FAT167	\$1.18
AngloGold (AGG)	-11.9%	\$10.90	FAT174	\$9.6
Hutchison (HTA)	-16.7%	\$0.42	FAT192	\$0.35
OceanaGold (OGD)	-18%	\$1.00	FAT169	\$0.82
Collection House (CLH)	-20.5%	\$2.10	FAT164	\$1.67
Hutchison (HTA)	-27.1%	\$0.48	FAT188	\$0.35
Minerals Corp (MSC)	-42.3%	\$0.13	FAT176	\$0.075
Minerals Corp (MSC)	-46.4%	\$0.14	FAT165	\$0.075
Henry Walker	-52.2%	\$0.90	FAT197	\$0.43

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While some may disagree, we believe 2004 has generally proven to be a solid year for Fat Prophets' Members. For those that did suffer realised or unrealised losses during the year, rest assured we will be working very hard to deliver exciting opportunities in 2005.

On the business front, the company continued to make considerable progress in the United Kingdom. The Fat Prophets UK portfolio delivered hypothetical returns of around 26 percent this year, which was considerably better than the broader market. Fat Prophets Mining also continued to make positive headway. In the first quarter of 2005 we have exciting plans to launch Fat Prophets Funds Management. We also aim to deliver further enhancements to the website in the year ahead.

Continuing an ongoing tradition at Fat Prophets, we have once again invited Members to award us a grade between A and D. An A being excellent and a D representing a very poor effort. As evidenced by the 2004 report card, Members on balance have been very content with our performance with a "B" being the average grade awarded. While satisfied, we will be striving to improve on this result in the next twelve months. We extend our thanks to all those who voted and provided feedback, both the good, bad, and even the ugly!

We wish all Member's a happy and safe Christmas, and of course a very prosperous New Year.

Signing off for 2004, we take this opportunity to thank you for your continued support.

Best wishes,

The Fat Prophets Team

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