

Dear Members,

The venerable John Pierpont (JP) Morgan was one of America's stock market forefathers. Following an extreme bout of volatility on Wall Street early last century, JP was asked by a panic stricken journalist about where stocks were headed. Famous for cutting to the chase, the wise old sage replied, "they will fluctuate".

"While some may disagree, we believe 2006 has generally proven to be a solid year for Fat Prophets' Members."

Nothing much has changed in 100 years. Stocks will always fluctuate and one of the great secrets, or disciplines, of course, is not to be overly surprised when they do. And 2006 has certainly been a year of stock price fluctuations.

The year began with commodity markets and related stocks on fire. Base metals, precious metals and oil all experienced strong gains in the first half of the year. Then we had the inevitable correction... and prices certainly fluctuated.

The correction ensured commodities were no longer the flavour of the month and investors began to look elsewhere for gains. Enter the private equity phenomenon and the second half of the year become all about picking the takeover target.

While the returns from investing in a company that has benefited from private equity interest have certainly been outstanding, we remind Members that this is not an investment strategy we subscribe to. The current situation is starting to remind us of 1986, or even 1999. We'll have more on this in our outlook piece, which we publish early in the new year.

In our opinion, the surge in global liquidity and investors' almost unswerving faith that inflation is not an issue is the driving force behind the markets' recent gains. Low inflation expectations mean interest rates expectations also remain low, and companies are therefore encouraged to increase their debt levels. Such financial engineering, and the prospect of more to come, certainly gave the market a boost this year.

The spate of private equity deals may have dominated the headlines in the latter half of 2006, but we continued to focus on commodities (specifically gold and oil stocks) and undervalued industrial stocks, both large and small. This has been to our detriment in the short term, with many of our recommendations remaining out-of-favour during the year.

So the market doesn't agree with our assessment, which, to be honest, suits us fine. The best long-term opportunities arise when a stock or sector is out-of-favour. It can be difficult going against the crowd initially,

but contrarian investing is not meant to be easy!

Big resource stocks like BHP are trading on single digit price to earnings (PE) multiples, despite remaining highly profitable and generating heaps of cash. This indicates many investors think commodities have had their day.

In fact, companies like BHP and Woodside Petroleum have gained little ground this year despite underlying commodity prices rising strongly. Even with these price rises, the global appetite for natural resources has showed little sign of abating.

And a passing fad this is not. Although emerging super economies such as China and India will experience the odd growth hiccup, their respective booms are real. Put simply, these nations are rebuilding themselves from the ground up and this of course requires a massive amount of infrastructure - from super highways to buildings and fibre optic cables.

A visit to Dubai earlier this year confirmed in our minds what is going on with the rise in commodity prices. The boom is not just about the rise of China, but also the massive flood of US dollar liquidity engulfing the world. Oil producing nations like the United Arab Emirates have seen the value of their primary export - oil, quadruple over the last five years.

Little wonder that these 'petrodollars' are now being spent by a host of newly enriched countries. And therein lays the problem for the greenback in future years.

Too much money chasing too few goods!

In the history of time, fiat currency (otherwise know as paper money) has been able to withstand excessive creation or money printing, because the scarcity factor (which ultimately is the fundamental factor that gives money its value), dissipates and confidence is lost.

The desire to rush out and turn that fiat currency into something 'tangible' first becomes real, and then turns into fear. And this road ultimately leads to panic. Money in the United States has not reached this state yet, but if the Federal Reserve and Government continue to sanction excessive money printing, there is no doubt in our mind that at some point, the dollar will endure a debilitating decline.

Which is why we continued to recommend gold related exposures later in the year, after the vicious gold price correction that began in May appeared to have worn itself out. Gold is a currency, not a commodity, and we believe the precious metal represents the ultimate insurance against the potential destruction of paper currencies.

Gold has been a cornerstone of the Fat Prophets Portfolio for many years. In fact, we first recommended the yellow metal in early 2001 at around US\$255 an ounce. At the time, many investment bankers dismissed gold as a "barbarous relic" with no relevance in the world economic monetary system.

Gold continued to defy the investment bankers in 2006, as it roared to US\$730 an ounce in May. We remain firm in our conviction that gold prices will rise well beyond US\$1000 an ounce in future years, and possibly as soon as next year! Be sure to check out our outlook piece on gold early in the new year.

During the year we attempted to selectively lock in profits across the portfolio when valuations were high. This is the definitive path of the value investor. If the market proves volatile in the year ahead, we are

confident that buying opportunities will emerge and it is therefore imperative that investors have access to sufficient cash reserves to buy when the timing is appropriate.

With respect to the Fat Prophets Portfolio, 8 out of the 12 stocks sold during the year yielded profits on the original recommended buy price.

Company	Return	Buy	Issue	Sell	Issue
MYOB (MYO)	#101.7%	\$0.60	FAT53	\$1.115	FAT307
Emperor Mines (EMP)	-52.4%	\$0.37	FAT51	\$0.20	FAT307
Village (VRL)	#75.4%	\$1.74 (ave)	FAT57	\$2.64	FAT304
Burns Philp (BPC)	96.4%	\$0.56	FAT124	\$1.10	FAT296
Auspine (ANE)	#128.2%	\$2.25	FAT124	\$4.17 (half)	FAT295
Downer EDI (DOW)	#157.9%	\$2.40	FAT128	\$5.71	FAT291
Austar United (AUN)	186.3%	\$0.454 (ave)	FAT24	\$1.30 (half)	FAT290
Ansell (ANN)	#163%	\$4.00	FAT54	\$10.00 (half)	FAT280
Minerals Corp.	-84.4%	\$0.154	FAT69	\$0.024	FAT277
MSC+MSCO	-55%	\$0.02	FAT197	\$0.009	
Paperlinx (PPX)	#-13.8%	\$4.72	FAT174	\$3.62	FAT270
AWB (AWB)	#-14.2%	\$4.80	FAT221	\$3.83	FAT269
Village (VRL)	#42.1%	\$1.74 (ave)	FAT57	\$2.40 (half)	FAT263

Denotes: # dividend included; (half) sold half

In terms of our recommendations for 2006, the results were a bit of a mixed bag. The mid year correction in the commodity sector has continued, impacting market sentiment towards many stocks in the portfolio. Furthermore, the drought played havoc with our agricultural recommendations, which were based on our long term bullishness towards agricultural commodity prices.

With a focus on contrarian opportunities, the markets in 2006 have provided slim pickings. In times of market euphoria, and consequent lack of value, our performance invariably suffers. This year has proven no exception.

However, we refuse to be drawn into 'flavour of the month' investing and will continue to focus on opportunities that we believe will deliver value over the long term.

Company	Return	Buy	Issue	Closing Price 18 December
Everest Babcock & Brown	#76.3%	\$1.435	FAT264	\$1.84

(EBB)				
T3	35.5%	\$2.00	FAT298	\$2.71
(TLSCA)				
Lihir Gold	32.6%	\$2.30	FAT265	\$3.05
(LHG)				
Foster's Group	#25.7%	\$5.54	FAT262	\$6.75
(FGL)				
Everest Babcock & Brown	#23.2%	\$1.493	FAT288	\$1.84
(EBB)				
McGuigan Simeon Wines	#22.2%	\$2.70	FAT297	\$3.30
(MGW)				
Sino Gold	20.3%	\$4.92	FAT301	\$5.92
(SGX)				
Indophil Resources	20.0%	\$0.60	FAT266	\$0.72
(IRN)				
Everest Babcock & Brown Invest. Trust	19.6%	\$3.52	FAT294	\$4.21
(EBI)				
Burns Philp	18.3%	\$0.93	FAT278	\$1.10
(BPC)				
Babcock & Brown Japan Property Trust	#16.1%	\$1.68	FAT285	\$1.95
(BJT)				
Salmat	15.8%	\$3.36	FAT301	\$3.89
(SLM)				
Rubicon Eurpoe Trust	#14.7%	\$0.97	FAT293	\$1.09
(REU)				
Lion Selection Group	#11.8%	\$1.82	FAT302	\$1.70
(LSG)				
Lihir Gold	10.9%	\$2.75	FAT301	\$3.05
(LHG)				
Babcock & Brown Capital	9.6%	\$3.96	FAT297	\$4.34
(BCM)				
BHP Billiton	#9.1%	\$23.96	FAT262	\$25.67
(BHP)				
Telstra	#9.0%	\$4.11	FAT265	\$4.14
(TLS)				
Telstra	#8.4%	\$3.95	FAT276	\$4.14
(TLS)				
Rubicon Japan Trust	7.5%	\$1.00	FAT299	\$1.075
(RJT)				
Macarthur Coal	#7.3%	\$5.06	FAT286	\$5.25
(MCC)				
Platinum Japan Fund	#3.6%	\$2.6076	FAT282	\$2.4775
(Unlisted)				
AuSelect	3.1%	\$1.13	FAT306	\$1.165
(AUS)				

IAG (IAG)	2.1%	\$6.06	FAT306	\$6.19
BlackRock Merrill Lynch Gold Fund (Unlisted)	1.5%	\$1.3976	FAT300	\$1.4183
Corporate Express (CXP)	#-0.2%	\$6.00	FAT279	\$5.90
Lion Selection Group (LSG)	#-1.3%	\$1.96	FAT272	\$1.70
Oil Search (OSH)	-3.3%	\$3.36	FAT299	\$3.25
Global Mining Investments (GMI)	-4.1%	\$1.33	FAT300	\$1.275
Ancor (AMC)	#-4.7%	\$7.70	FAT271	\$7.17
Oceania Gold (OGD)	-5.1%	\$0.69	FAT304	\$0.655
IAMGOLD (IGD)	-6.7%	\$1.20	FAT306	\$1.12
IAMGOLD (IGD)	-8.2%	\$1.22	FAT273	\$1.12
Oil Search (OSH)	#-8.8%	\$3.65	FAT268	\$3.25
BHP Billiton (BHP)	-9.1%	\$28.23	FAT302	\$25.67
Newmont Mining (NEM)	-9.1%	\$6.68	FAT291	\$6.05
SP Telemedia (SOT)	-12.6%	\$0.91	FAT302	\$0.795
Queensland Cotton (QCH)	#-13.8%	\$4.00	FAT270	\$3.23
Newmont Mining (NEM)	-14.5%	\$7.10	FAT281	\$6.05
GRD (GRD)	-14.9%	\$2.35	FAT284	\$2.00
Westonia Mines (WEZ)	-17.6%	\$0.17	FAT263	\$0.14
Queensland Cotton (QCH)	#-19.8%	\$4.30	FAT277	\$3.23
AWB (AWB)	#-20.2%	\$4.80	FAT263	\$3.83
Westonia Mines (WEZ)	-33.3%	\$0.21	FAT278	\$0.14
Tap Oil (TAP)	-34.3%	\$2.20	FAT275	\$1.445
Fone Zone	-36.0%	\$1.25	FAT306	\$0.80

(FZN)

Tap Oil **-38.5%** \$2.35 FAT267 \$1.445

(TAP)

Emperor Mines **-52.4%** \$0.42 FAT268 \$0.20

(EMP)

While some may disagree, we believe 2006 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 2007.

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 2006 Report Card, Members on balance have been satisfied with our performance with a 'B' being the average grade awarded. We hope to go one better in 2007 as we are looking to make improvements in a number of areas next year. 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 2006, we take this opportunity to thank you for your continued support.

Best wishes,

Fat Prophets

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