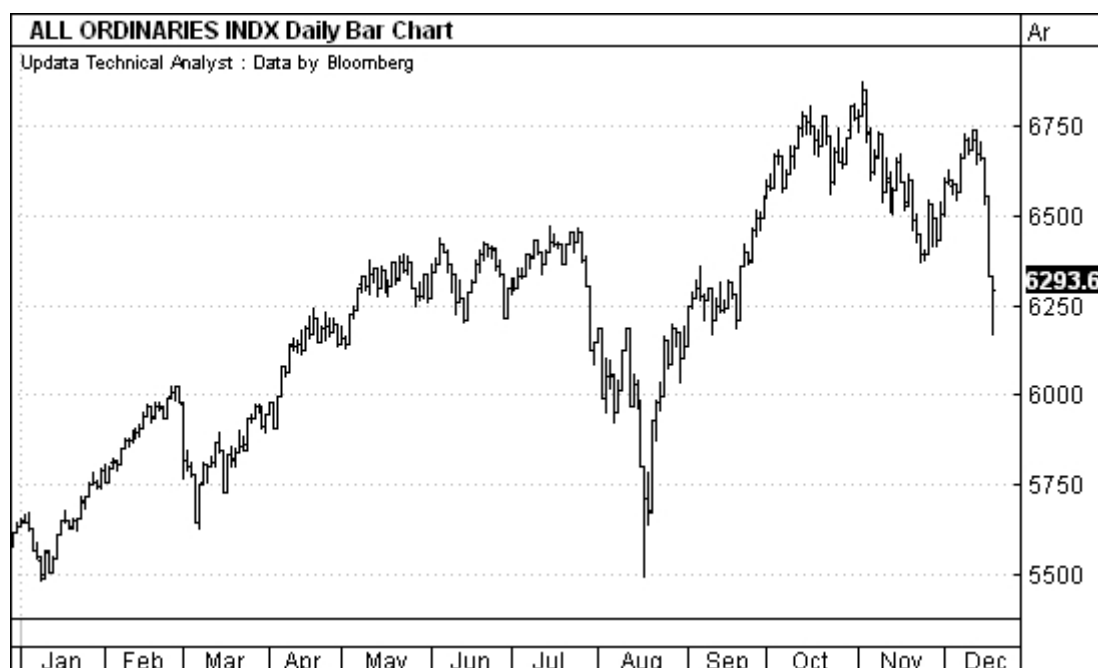


Well, this year has certainly been an extraordinary one for investors. In our 2007 outlook piece, we highlighted that volatility would be a defining characteristic of the year given the amount of debt and leverage in the global financial system, and that has certainly proven to be the case.

We were perhaps too bearish at the start of the year, as we thought that while the market might swing around wildly, returns would be flat. Despite the current late year sell-off, the All Ords is still up around 10 percent, not including dividends. Whether the market can hold on to these gains for the last few weeks remains to be seen.



Our main theme for the year has been to favour resources, or 'real' assets, over financials or 'paper' based assets. This has broadly played out, although not without considerable volatility.

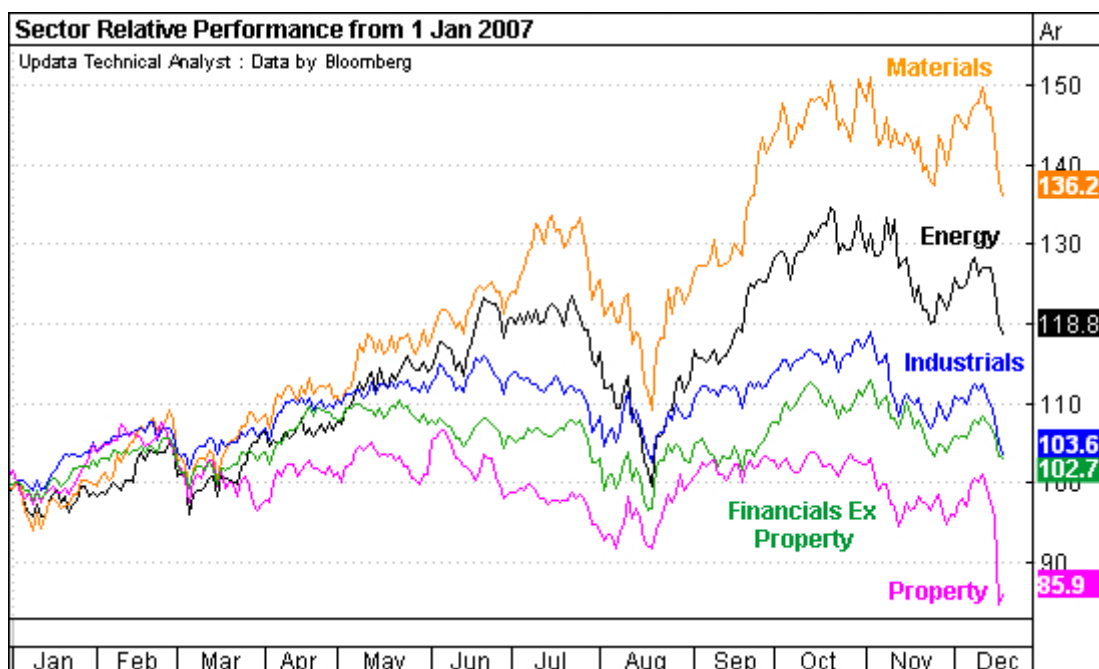
The year began on shaky ground with oil and commodity prices in general falling. At the start of the year, the oil price reached a low of US\$49.90 and many investors expected it to continue falling. However, as the chart below shows, that wasn't to be. We maintained an US\$80 price target at the start of the year and to many investors' surprise, oil breached that limit easily and even challenged the US\$100 mark.



As the hype around private equity began to simmer, investors soon began to realise that resource stocks represented fundamentally good value, and the sector enjoyed a significant re-rating. Essentially, this means investors were happy to pay, for example, 15 times for a company's earnings rather than 9 times as was the case earlier in the year. In this example, the 're-rating' accounts for a 66 percent share price gain without a change in earnings.

Of course this didn't happen to all stocks in the sector. Many miners fell victim to high costs and shrinking margins, and despite high commodity prices, profitability remained constrained for many companies.

Despite this, the materials (or resources) sector was the standout performer of the year, no doubt led by the strong performance of heavyweights BHP Billiton and more recently Rio Tinto. As shown in the chart below, the materials and energy sectors have comfortably outperformed the industrials and financial sectors this year.



The main reason for this underperformance is due to the fact that these sectors were 'priced for perfection' at the beginning of the year. Private equity involvement in most industrial sectors pushed prices well above fair

value and the belief in feely available and cheap credit (debt) saw financials and leveraged infrastructure companies all trading at very optimistic levels.

In stark contrast to many of the resource stocks, industrials and financials have undergone somewhat of a 'de-rating' throughout 2007. We are quite pleased with this development, as it provides many opportunities for 2008.

While we will discuss these in more detail in our outlook piece (to be published in the second week of January) we believe that there are emerging pockets of value in the industrial sector...a situation we have not seen for some time.

As we expected, 2007 was another strong year for gold. While gold has gained increased acceptance as an investment over recent years, we still detect great scepticism from the wider investment community over the merits of gold.



We believe this is a strong indication that gold is still in the midst of a bull market. Real and enduring bull markets tend to confound the sceptics and we do not think gold will prove any different.

However, while there are still sceptics, gold stocks will always be considerably more volatile than the market. We have seen such volatility in the past few days, despite the Aussie dollar gold price remaining firm. We encourage Members not to be shaken out of their positions because of wild price swings, but rather to remain focussed on the underlying picture, which continues to be bullish for gold.

From a big picture perspective, we are pleased to say we saw the US housing slowdown and associated credit issues coming from a mile away and have attempted to minimise any exposure to these related events.

Of course, when the market is in panic mode, as has been the case recently, both good and bad companies face selling pressure. However, we remain confident that we have avoided the worst of the credit market issues in terms of our recommendations.

We took profits on a number of our positions this year, in addition to booking a few losses. For new Members, keep in mind we tend to hold stocks for a multi year period, in order to let our investment thesis play out.

Although it's always tempting to take profits after a stock has gained 10 or 20 percent, or to cut losses after a similar fall, we wholeheartedly believe that this is the road to achieving mediocre returns.

The table below details our sell and sell half recommendations completed throughout the year. The 'return' column is the total return from our initial buy price or average entry price, including dividends.

We took some profits or exited many of our longer held positions throughout the year for some solid gains. On the downside, we took a large loss on Mcguigan Simeon Wines. For more detail on the reasons behind our selling decisions, please refer to 'Where we took profits and cut losses in 2007', including in this week's report.

Stock	Purchase Price*	Buy	Sale Price	Sale	Simple return	Annualised Return
		Issue		Issue		
ANN	4.000	FAT54	11.460	FAT312	202.00%	38.58%
QBE	4.900	FAT48	30.750	FAT312	579.69%	108.51%
BJT	1.285	FAT227	2.060	FAT313	74.13%	42.48%
QCH	4.000	FAT270	3.300	FAT314	-12.00%	-13.31%
IGD**	0.591	FAT120	1.050	FAT315	78.88%	19.87%
HTA	0.480	FAT188	0.215	FAT318	-55.21%	-20.86%
BSG	1.040	FAT257	2.990	FAT326	188.94%	132.88%
HHL	1.390	FAT21	12.900	FAT327	952.16%	153.64%
ANE	2.250	FAT22	6.110	FAT327	202.00%	32.70%
ABB	6.790	FAT239	8.360	FAT329	29.60%	16.05%
TWR	0.686	FAT67	2.120	FAT329	217.09%	40.70%
AMC	5.250	FAT1	7.390	FAT330	79.43%	11.90%
REU	0.970	FAT293	0.965	FAT338	9.23%	9.99%
CXP	6.000	FAT279	6.300	FAT339	8.58%	7.09%
AMP	7.790	FAT21	10.160	FAT342	76.12%	11.74%
EBB	1.380	FAT248	3.450	FAT316	200.00%	143.14%
EBB	1.380	FAT248	1.990	FAT345	99.06%	50.15%
IWL	2.160	FAT202	6.380	FAT346	233.33%	80.04%
MGW	3.350	FAT244	2.230	FAT330	-27.99%	-15.84%
MGW	3.350	FAT244	1.760	FAT346	-42.01%	-20.28%
BCM	3.950	FAT297	4.810	FAT349	21.77%	20.22%
CTX	2.150	FAT31	20.290	MWA	950.70%	146.73%

* Purchase price refers to the initial purchase price, or 'average' purchase price when a stock has been subsequently recommended as a buy to all Members **Initial exposure gained through Gallery Gold

With respect to our recommendations in 2007, we had some solid hits this year but too many misses. Newcrest Mining was a well-timed buy among others and our recommendation to buy many large cap resource stocks at the height of volatility in August proved a profitable call.

However, we are disappointed that many of our other recommendations were wide of the mark, at least in the short term. For example, we thought the insurers looked like good value in a heated market and soon after buying, both IAG and Suncorp suffered a harsh claims environment from storms and floods. And in IAG's case, the performance of the UK business has not met early expectations.

Sp Telemedia was another disappointment. Despite having one of the few fibre infrastructures in the telco industry, management have been unable to build scale and profitability has suffered.

Despite these setbacks, we remind ourselves constantly that we are investing in companies, not share prices, and when a company encounters hurdles on the operational front, things do take time to get back on track.

Below we include a table of our current portfolio. We show year-to-date returns as well as returns since inception, both total and annualised.

Ticker	Name	Initial Buy Issue	2007 Return	Total Return-Annualised	Total Return-Holding Period
HHL	HUNTER HALL INTERNATIONAL LT	FAT21	31.45	54.03	1775.45
MCC	MACARTHUR COAL LTD	FP98	76.95	53.90	870.43
QBE	QBE INSURANCE GROUP LIMITED	MWA	14.52	40.00	716.75
MLE	MACQUARIE LEISURE TRUST GROU	FAT82	14.01	42.42	618.71
LGL	LIHIR GOLD LTD	FP8	-0.32	27.86	469.00
WPL	WOODSIDE PETROLEUM LTD	FP7	27.50	26.01	415.43
NUF	NUFARM LTD	FP102	39.91	35.96	390.29
PDN	PALADIN ENERGY LIMITED*	FP255	-30.03	187.09	386.47
OSH	OIL SEARCH LTD	FP59	35.42	29.86	384.50
IRN	INDOPHIL RESOURCES NL	FAT80	14.81	31.72	370.00
NEM	NEWMONT MINING*	FP3	-6.25	25.85	185.34
RSG	RESOLUTE MINING LTD	FP70	1.05	19.71	185.31
GRD	GRD LTD	FAT117	7.75	19.26	135.74
ASB	AUSTAL LIMITED	FP85	-25.43	14.51	111.31
LST	LION SELECTION LTD*	FP31	-3.41	16.76	110.19
BHP	BHP BILLITON LTD	FAT262	60.38	39.88	95.67
FGL	FOSTER'S GROUP LTD	FAT150	-4.46	13.86	84.46
DIO	DIORO EXPLORATION NL	FAT3	56.70	8.79	82.89
TLSCA	TELSTRA CORPORATION-INS RECP	FAT298	15.13	59.01	70.00
GMI	GLOBAL MINING INVESTMENTS	FAT251	71.94	51.98	61.51
TAL	TOWER AUSTRALIA GROUP LTD*	FAT304	-18.69	51.21	55.00
NAM	NAMOI COTTON CO-OPERATIVE	FP29	-21.44	6.47	51.34
MLIGF	Merrill Lynch International Gold Fund	FAT255	-6.52	22.96	47.49
BJT	BABCOCK & BROWN JAPAN PROPE	FAT227	-32.67	13.46	39.30
TOX	TOX FREE SOLUTIONS LIMITED	MWA	38.86	48.12	38.86
TLS	TELSTRA CORP LTD	MWA	22.25	9.33	29.19
ORI	ORICA LTD	FAT315	27.87	33.95	27.87
SLM	SALMAT LTD	FAT301	5.50	23.60	27.01
NCM	NEWCREST MINING LIMITED	FAT343	25.26	122.12	25.26
SGX	SINO GOLD MINING LTD	FAT301	-15.48	21.69	24.80
WOTCA	WESTPAC OFFICE TRUST-PP	FP219	10.45	6.97	20.76
OXR	OXIANA LTD	MWA	18.76	31.38	18.76
PLATJPN	PLATINUM JAPAN FUND-C	FP230	-12.63	5.93	15.93
DWSGWAG	DWS GLOBAL EQ AGRIBUSINESS	FAT324	11.59	18.40	11.59
AWE	AUSTRALIAN WORLDWIDE EXPLORA	FAT322	-1.97	13.05	9.06
BCM	BABCOCK & BROWN CAPITAL LTD	FAT297	-7.22	1.64	2.01
SBM	ST BARBARA LTD	FAT232	1.61	2.42	1.61
CXC	COUER D'ALENE MINES*	FAT353	1.10	14.86	1.10
PTM	PLATINUM ASSET MANAGEMENT	FAT324	-0.40	-0.62	-0.40
EBI	EVEREST B&B ALTERN INV TRST*	FAT288	-15.28	-1.55	-2.13
BDL	BRANDRILL LIMITED	FAT351	-6.76	-46.36	-6.76
AEZ	APN/UKA EUROPEAN RETAIL PROP	FAT319	-7.56	-9.77	-7.56
AVJ	AVJENNINGS LTD	FAT339	-15.00	-36.20	-15.00
SUN	SUNCORP-METWAY LTD	FAT328	-17.66	-28.78	-17.66
RJT	RUBICON JAPAN TRUST	FAT299	-30.84	-17.57	-20.50
TAP	TAP OIL LIMITED	FAT258	34.87	-13.38	-25.09
IAG	INSURANCE AUSTRALIA GROUP	MWA	-29.66	-24.52	-25.22
API	AUSTRALIAN PHARMA INDUS LTD	FAT328	-28.51	-44.92	-28.93
AVX	AVEXA LTD	FAT326	-29.37	-43.26	-29.37
BTA	BIOTA HOLDINGS LIMITED	FAT332	-31.28	-53.08	-31.28
FZN AU	FONE ZONE GROUP LTD	FAT306	-13.29	-37.61	-38.57
WFEZ	WESTONIA MINES LTD	FP	11.87	6.88	12.77

WEZ	WESTONIA MINES LTD	IFU	-44.97	-9.95	-42.77
SOT	SP TELEMEDIA LTD	FAT302	-35.64	-41.52	-44.86
OGC	OCEANAGOLD CORP-CDI*	FP169	-35.57	-18.50	-52.00

*Effective entry price used due to corporate actions

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 D representing a very poor effort. As evidenced by the 2006 Report Card, Members on balance have been satisfied with our performance this year, with a 'B' being the average grade awarded.

We extend our thanks to all those who voted and provided feedback; both the good, bad, and even the ugly! While we can't respond to all the comments, we do take note of your comments and we will be looking to make a number of improvements to the report next year.

If we haven't lived up to your expectations so far, we hope that our hard work will provide better rewards in 2008.

We wish all Members a happy and safe Christmas, and a very prosperous New Year.

Signing off for 2007, we take this opportunity to thank you for your continued support.

Best wishes,

Fat Prophets

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