

Where we took profits and losses in 2014

We continued with a strategy of ramping up portfolio management in 2014, and generally this worked out well. Below we provide a brief review of the stocks that we recommended either an outright exit (Sell) or a partial exit (Sell Half) from over the course of the year.

We made 23 sell and sell-half calls this year, with 18 of them resulting in positive gains and 5 resulting in losses to a various degree. The majority of stocks are currently trading at prices lower than our recommended exit price, but we continue to view the prospects for those positions where we recommended a sell half positively overall. Thus we are content to retain our reduced position.

We note that in the case of Donaco International and Programmed Maintenance we recommended Members partially exit the stocks earlier in the year and fully exit the position later in the year. Our calls by stock are provided below in reverse chronological order.

Graincorp

While we were of the view that Graincorp (ASX: GNC) looked cheap on a through-the-cycle basis given its dominant position along the eastern seaboard, we advised members to sell their entire holding in mid-November 2014 around \$8.02 per share.

This was based on our view that, while the business is seasonal in nature, Graincorp's balance sheet is vulnerable to another year of below-average grain volumes. This is expected to place downward pressure on earnings (and cash flow) at a time when the company also has significant capital expenditure requirements, thus suggesting to us that further equity and/or lower dividends may be required.

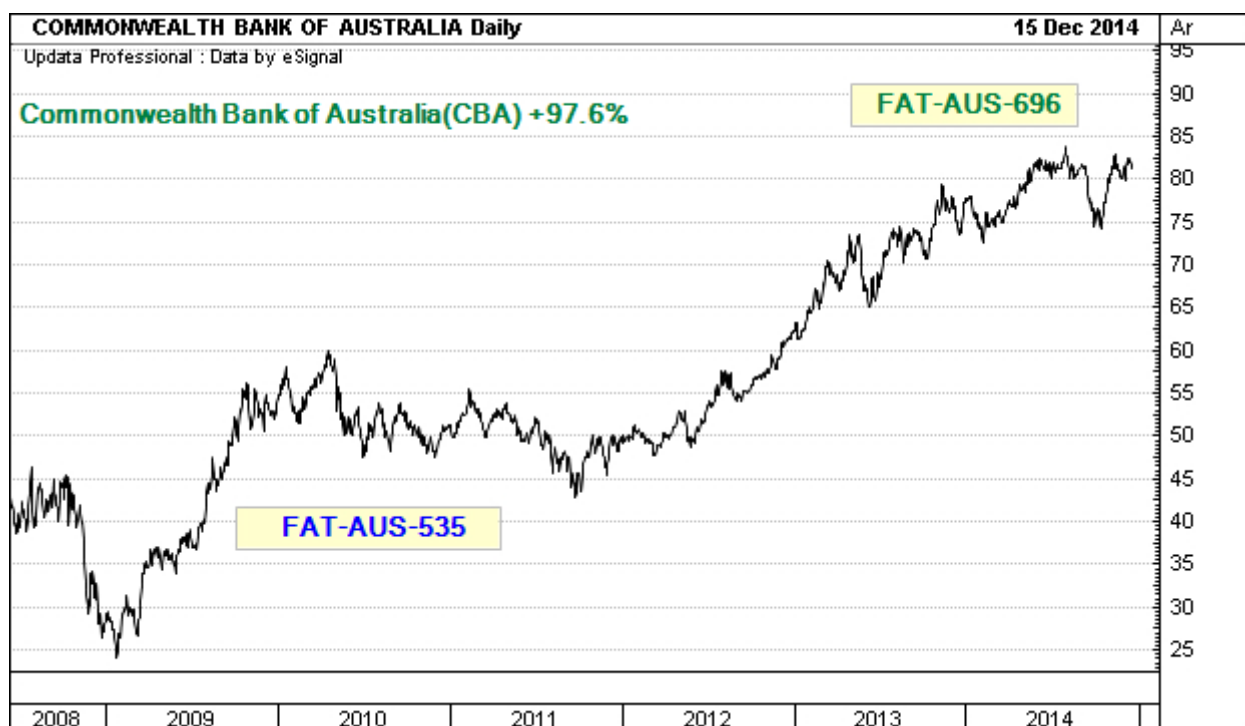
After having taken profits at higher prices when ADM was seeking to buy Graincorp, our final exit price represented a 18.9 percent gain, or 6.5 percent annualised on the initiation price.



Commonwealth Bank of Australia

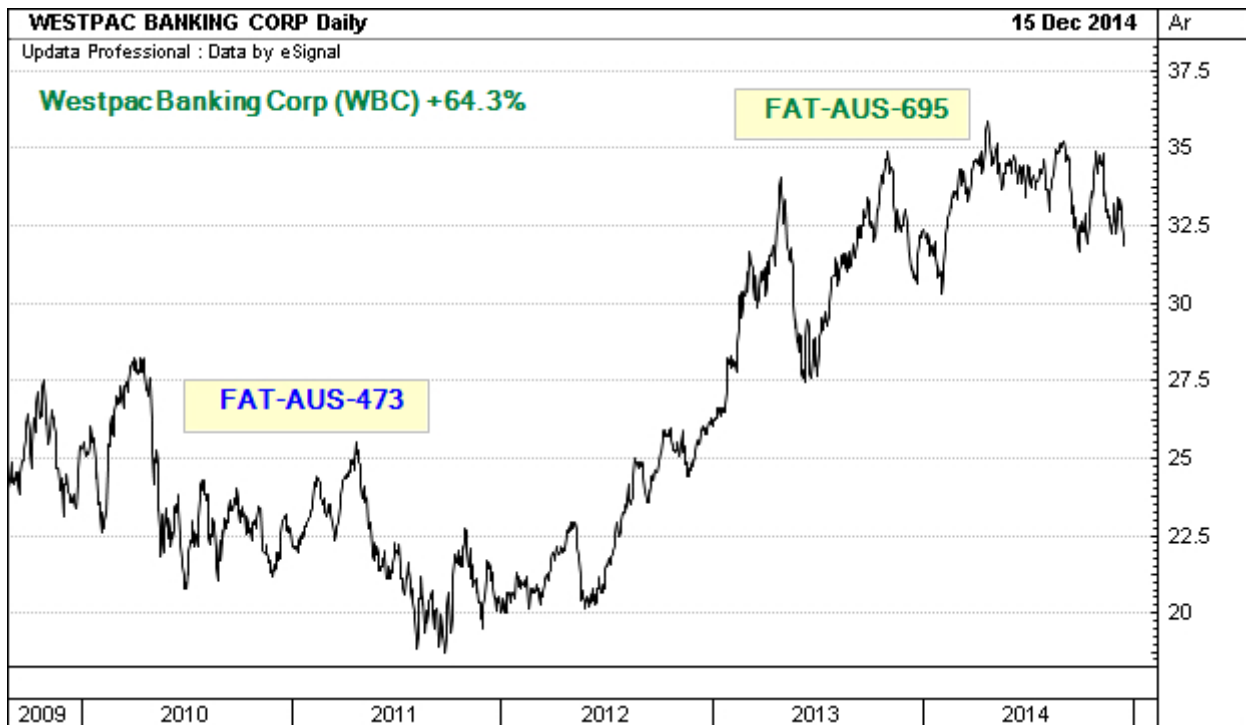
In late October 2014 we published a report recommending that members bank some of their profits in Commonwealth Bank of Australia (ASX:CBA) at around \$80.00 per share. This represented a return of 97.6 percent, or 23.5 percent annualised on our initial entry price.

The rationale for doing so was our view that CBA, along with its peers has already plucked much of the 'low hanging fruit' available to boost earnings. With the Big Four having achieved material improvements in productivity over the last several years through an investment in technology, we think the easy gains have now been made, with the prospect of a tighter regulatory environment also limiting the potential upside.



Similar to our view on the Commonwealth Bank of Australia, while Westpac (ASX: WBC) has been delivering solid earnings growth by focusing on productivity gains and clamping down on credit risks, we believe a lot of the easy gains have now been made.

Adding to the mix the potential for tighter regulatory controls, which will increase compliance costs and reduce returns on capital, we suggested that members take some profits (i.e. sell half of their holding) in WBC around \$33.34 per share. While we continue to view WBC as a good long-term exposure to the Australian banking sector, we felt it prudent to take some profits in October. The return on Westpac since entering the portfolio of 64.3 percent equated to an annualised gain of 11.8 percent.



ANZ

With our recent call to take some profits in the Big Four being predicated on macro factors, rather than any company specific event or issue, what held true for CBA and WBC also holds true for ANZ.

As such, in mid-October 2014, we recommended that members take some profits (i.e. sell half of their holding) in ANZ around \$31.15 per share. While noting that there is still much to like about ANZ, in particular its Asian growth potential, in the short term we see the upside for the bank being capped by relatively weak sentiment and most of the 'low hanging fruit' having already been plucked by the banks in the Australian market.

The exit price represented a return of 123.3 percent, or 16.6 percent annualised.



Programmed Maintenance

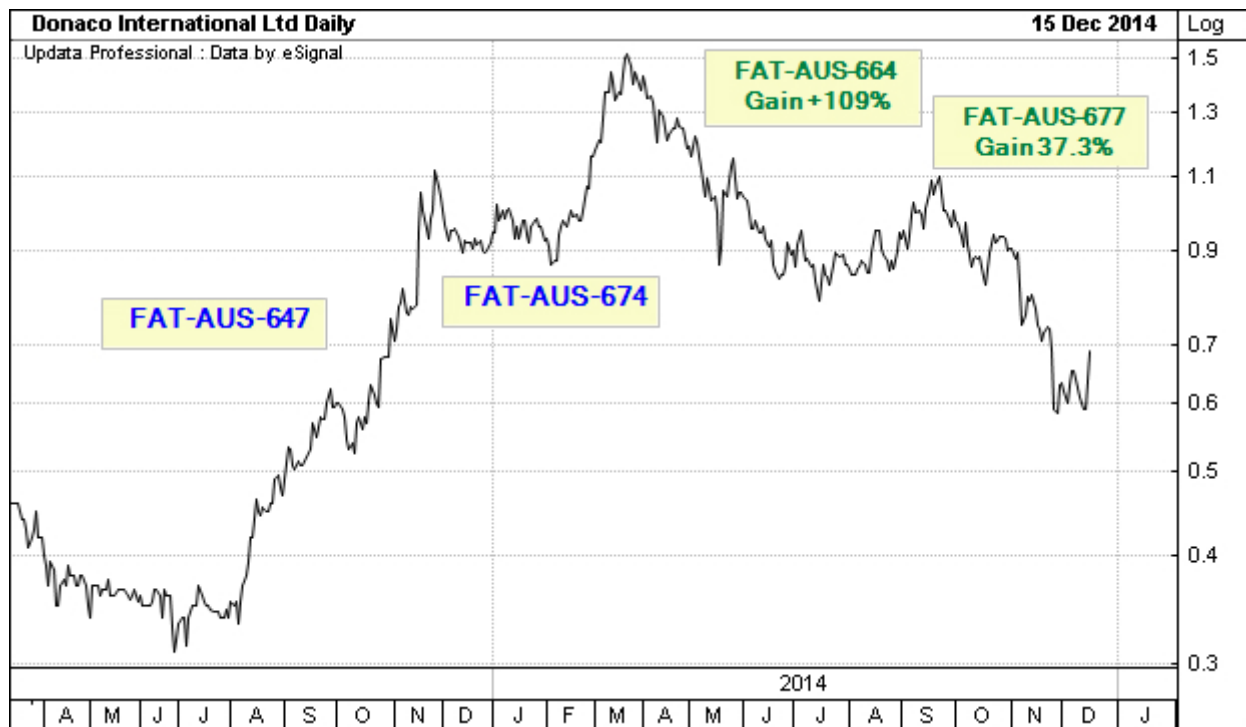
Having previously recommended to members that they take some profits in Programmed Maintenance (ASX: PRG) around \$2.93 back in April, we upped the ante in mid-October by recommending members exit the stock around \$2.51 per share.

This was based on our view that the relative outperformance of the company's shares compared to the broader market was arguably not justified given the ongoing deterioration in its underlying markets. With no clear catalysts to mitigate or offset the increasing headwinds facing the sector, we took the view that the company's earnings would not be able to justify the current share price.



In mid-June 2014 we recommended that members exit Donaco International (ASX: DNA) around \$0.925 per share on the basis that the company's relatively high valuation metrics were looking vulnerable to political instability in Asia and the more recent sell-off in Macau gaming stocks.

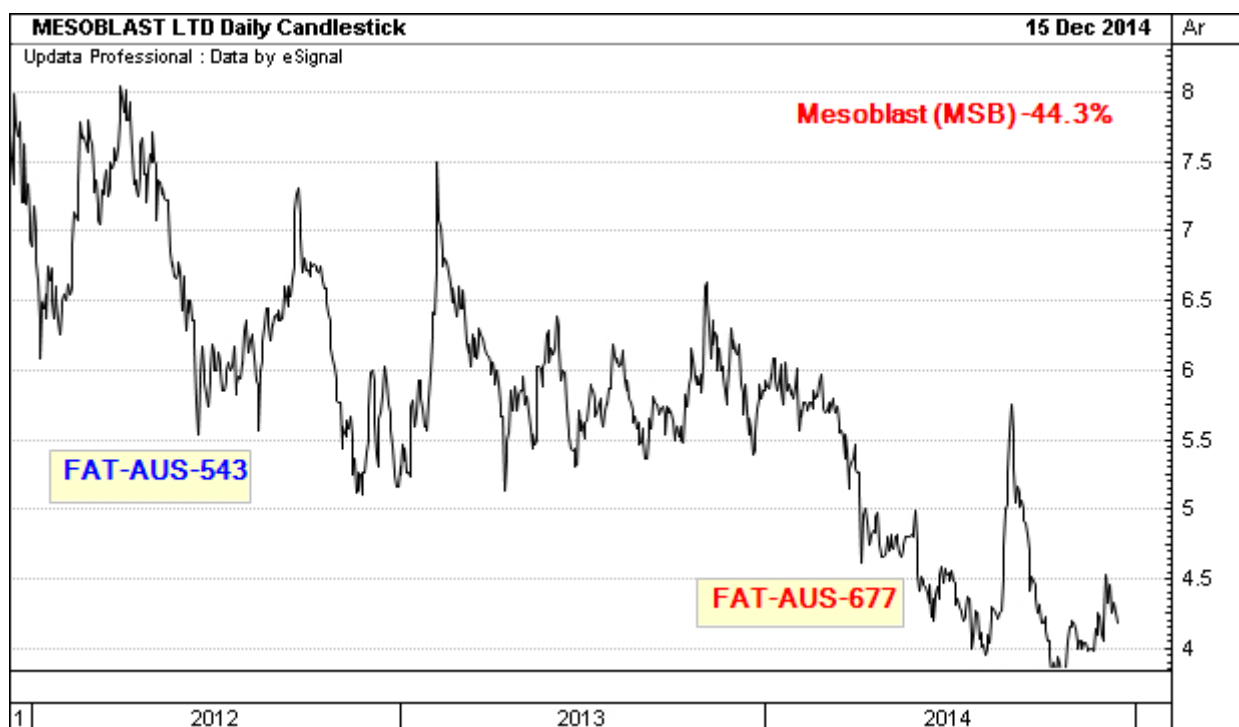
While we remain positive on the long term earnings growth potential of the company, as evidenced recently by the new Aristo International Hotel and casino property, we are also cognisant of the need to protect profits earned on the stock to date. Our decision to exit the stock followed our early call in March 2014 to take some profits around \$1.40 per share.



Mesoblast

Having initially recommended the stock to investors in October 2011 at around \$7.99 per share, it is reasonable to conclude that the investment has not been a good one. Within the context of generally weak sentiment towards biotechnology companies, Mesoblast's (ASX:MSB) share price was being depressed by the market's concern about its increasing rate of cash burn and lack of results in monetization of its prospects to date.

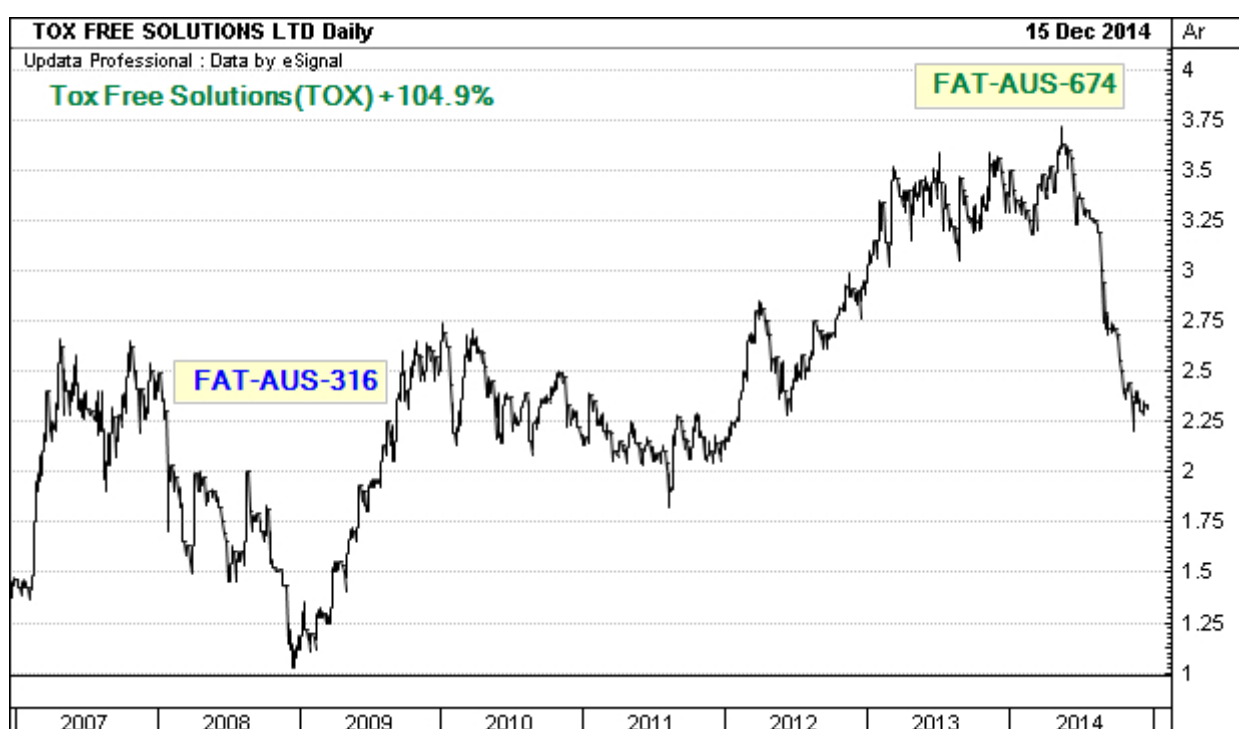
While this led to Mesoblast getting a 'please explain' letter (i.e. a speeding ticket) from the Australian Stock Exchange, our decision to exit the stock around \$4.45 per share was based on there being better opportunities (i.e. on a risk/reward basis) elsewhere.



Tox Free Solutions

Tox Free Solutions (ASX: TOX) has been something of a stalwart in the Fat Prophets portfolio in recent years having almost doubled since being recommended as an initial holding in February 2007 at \$1.85. However, with the stock having seemingly become a victim of its own success, there came a point in time when the company's earnings started to meet, rather than exceed, the market's expectations.

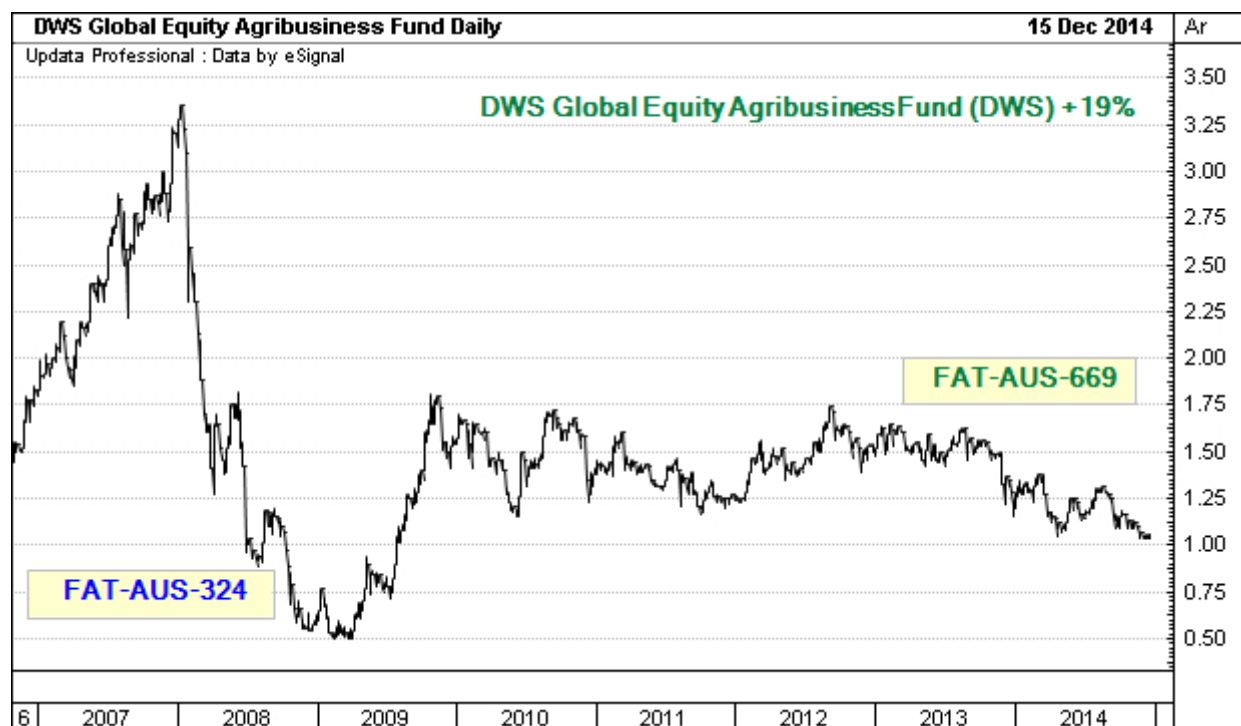
While we remain positive on the medium-term outlook for the company, our decision to exit the stock in late-May 2014 around \$3.62 per share was based on some emerging weakness in its underlying markets and some director selling. Our exit price from Tox in May represented a return of 104.9 percent, or 10.4 percent annualised.



The DWS Global Equity Agribusiness Fund was added to the Fat Prophets Portfolio as a play on our long term bullish view of soft commodity prices.

The Fund invests in all parts of the 'field to table' value chain through stakes in listed companies worldwide. Our thematic view was that soft commodity prices would enjoy the tailwind of a growing global population underpinning rising demand, against the backdrop of escalating supply constraints.

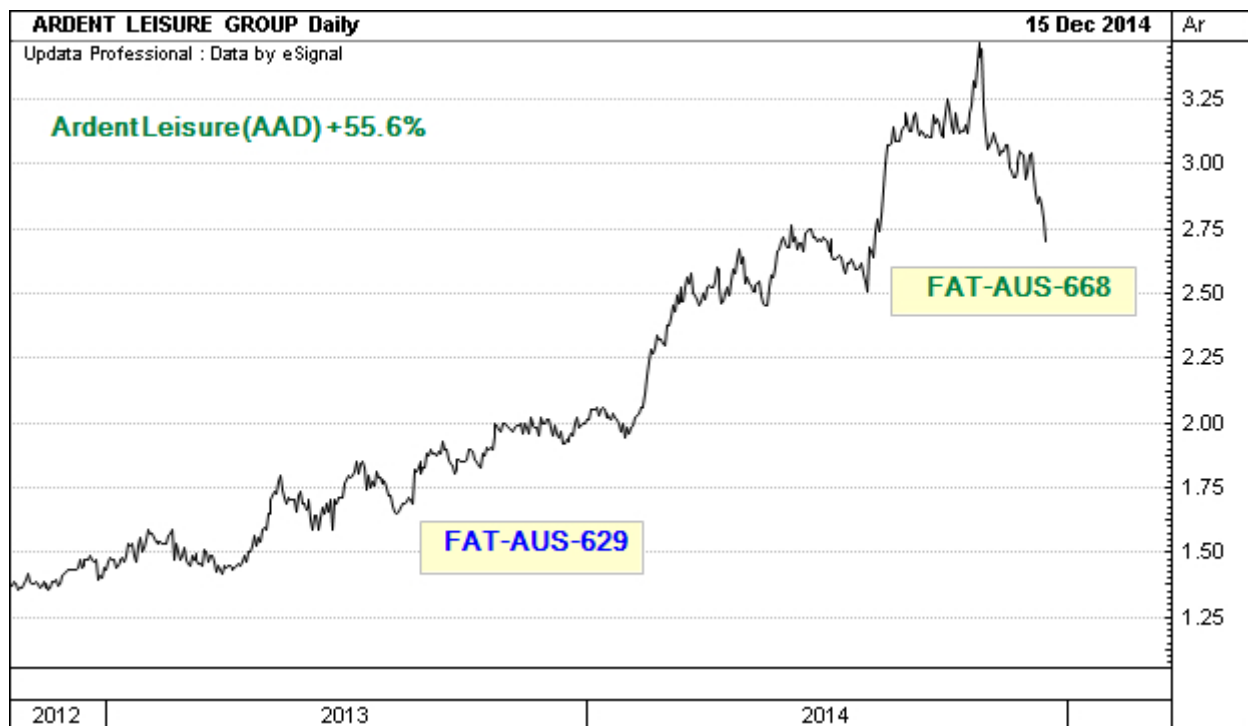
While this view remains unchanged, in mid-April 2014 we recommended that members exit the stock around \$1.00 per unit (initial \$1.07 per unit entry price) in preference for a more targeted approach. While our exit price was below our entry price, distributions resulted in a modest positive return from an absolute perspective.



Ardent Leisure

In early April 2014 we recommended that members take some profits in Ardent Leisure (ASX: AAD) around \$2.56 per share. This was in response to the 24 percent jump in Ardent Leisure's share price in the days following the release of a set of strong interim results.

While we remain of the view that the company outlook is positive, particularly in relation to Main Event and the Health Clubs divisions, with the company's shares having increased by 54 percent since being added to the Fat Prophets portfolio in June 2013, we thought it prudent to lock in some of these gains. Looking ahead, we expect further gains to be underpinned by a lower Australian dollar.

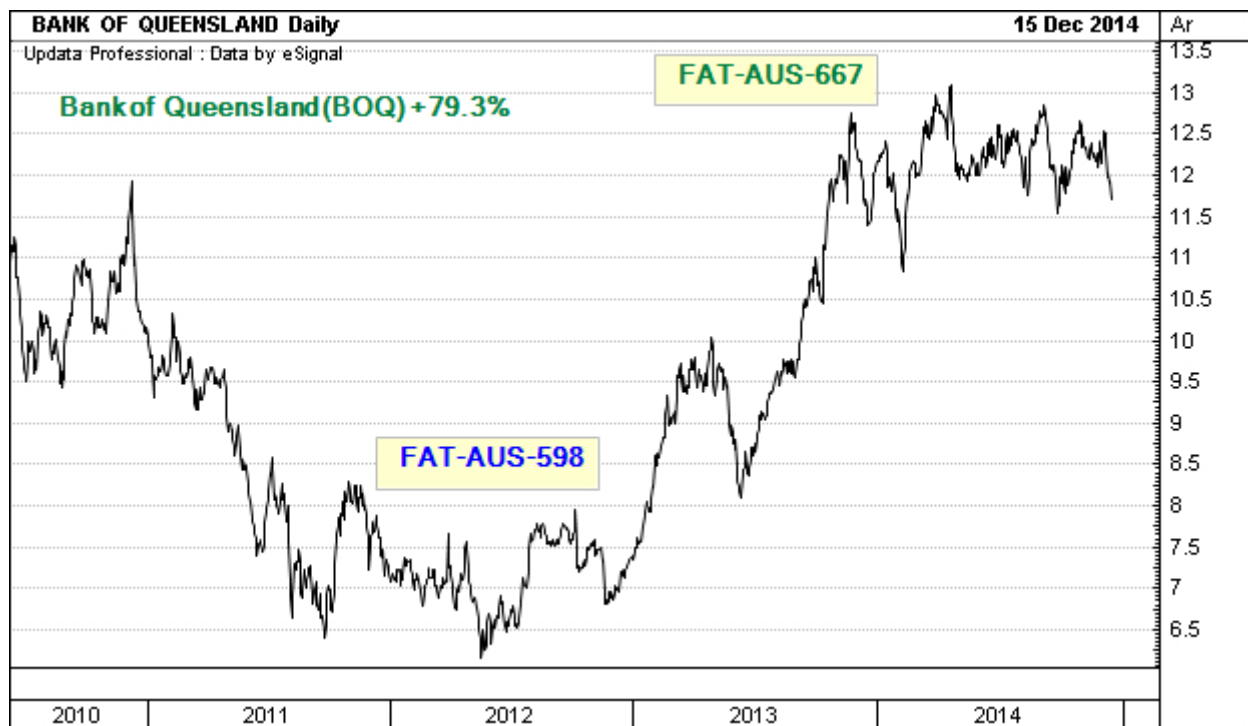


Bank of Queensland

We introduced the Bank of Queensland (ASX: BOQ) into the portfolio in October 2012 when it was the ‘ugly duckling’ of the domestic banking sector and had been under severe pressure on the back of a substantial jump in bad debt write-offs, and heavy exposure to weakness in the Queensland economy. Indeed, the bank had to go to the market with a \$450 million rights issue earlier that year to shore up its capital position.

Our investment thesis was based on an attractive valuation along with attractive solid dividend yield. In addition, we were encouraged by new management’s initiatives to spur growth and diversify organic earnings while at the same time tackling costs. Furthermore, we believed new controls over credit lending were likely to result in declining impairments and bad debts. Finally, we were attracted to the bank’s leverage to the revival of the Queensland economy.

Significant parts of our investment thesis have played out since that time and we viewed it prudent in April of this year to bank some gains, recommending Members sell half of their position at \$12.77. The absolute return at the time of the sell half recommendation of 79.3 percent equated to an annualised gain of 50.9 percent, inclusive of dividends, as per usual.



Resource Equipment

The resources industry has been volatile in the past 18 months or so, which by extension has meant that companies providing equipment and services to the industry have faced a very tough backdrop as their mining customers deferred projects and looked to reduce contractor costs.

When Resource Equipment (ASX: RQL) entered the portfolio in March 2011 at an initial entry price of \$0.70 per share we viewed its mine de-watering and water system management services as being much more defensive than how it seems to have played out. The company's services did not prove immune to the tough times facing the broader industry and we exited the stock in March of this year after the company reported a \$1.4 million loss in the six months to December 2013. This resulted in one of our larger losses compared to our effective entry point.



Seek

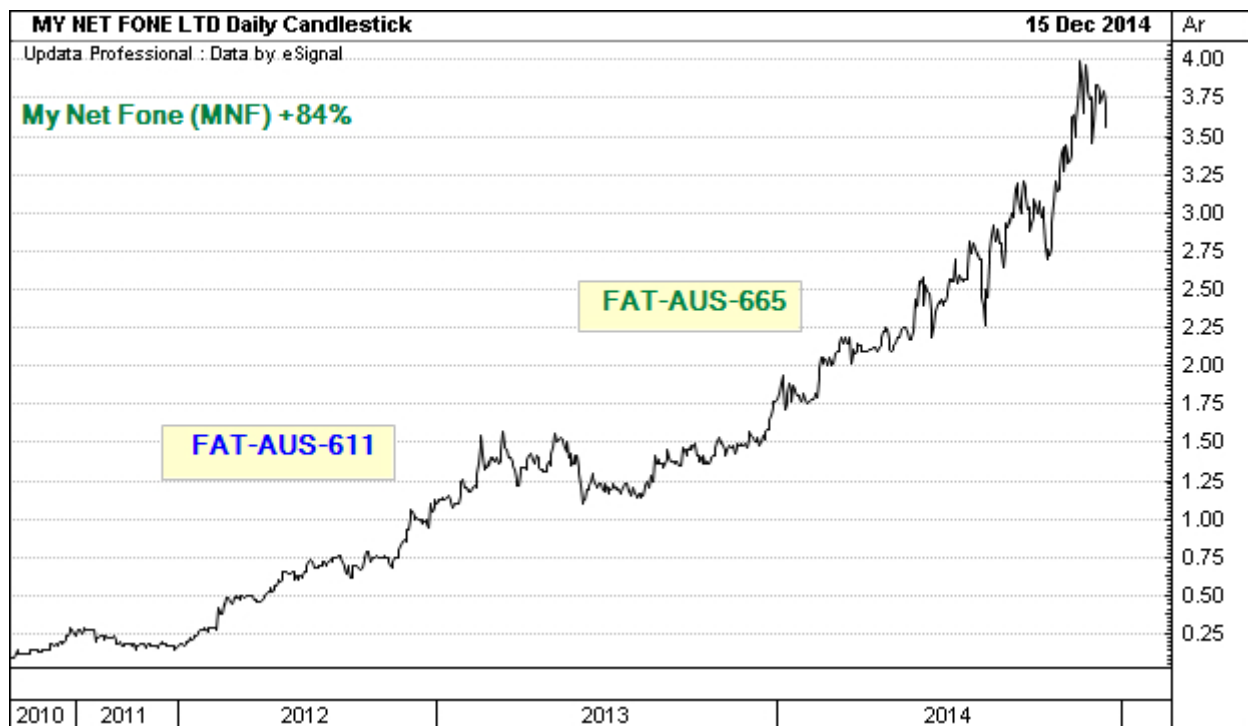
We introduced Seek (ASX: SEK) into the portfolio in April of 2009 at an initiation price of \$3.00 per share due to its dominant position in the domestic online job space and opportunities to replicate its model overseas.

Seek was a strong performing stock during its time in our portfolio, rising more than fivefold and we finally exited the position in March of this year at \$16.87, after having taken part profits on two previous occasions August 2009 (FAT-AUS-439) at \$5.35 and at \$9.97 in February 2013 (FAT-AUS-613) as the company's valuation metrics expanded.



My Net Fone

We took some profits on fast growing junior Telco, My Net Fone (ASX: MNF) in March of this year after the stock had rocketed up almost 80 percent since joining the portfolio at \$1.22 a little over a year earlier. While we continue to like the outlook for the company due to organic growth supplemented by bolt-on acquisitions, we felt it was prudent to take some profits off the table. We will however retain our reduced holding at this juncture.



Metcash

Metcash (ASX: MTS) joined the portfolio in May 2015 at a price of \$4.18 per share and we exited the position in March of this year, crystalizing a loss of 18.4 percent after accounting for dividends.

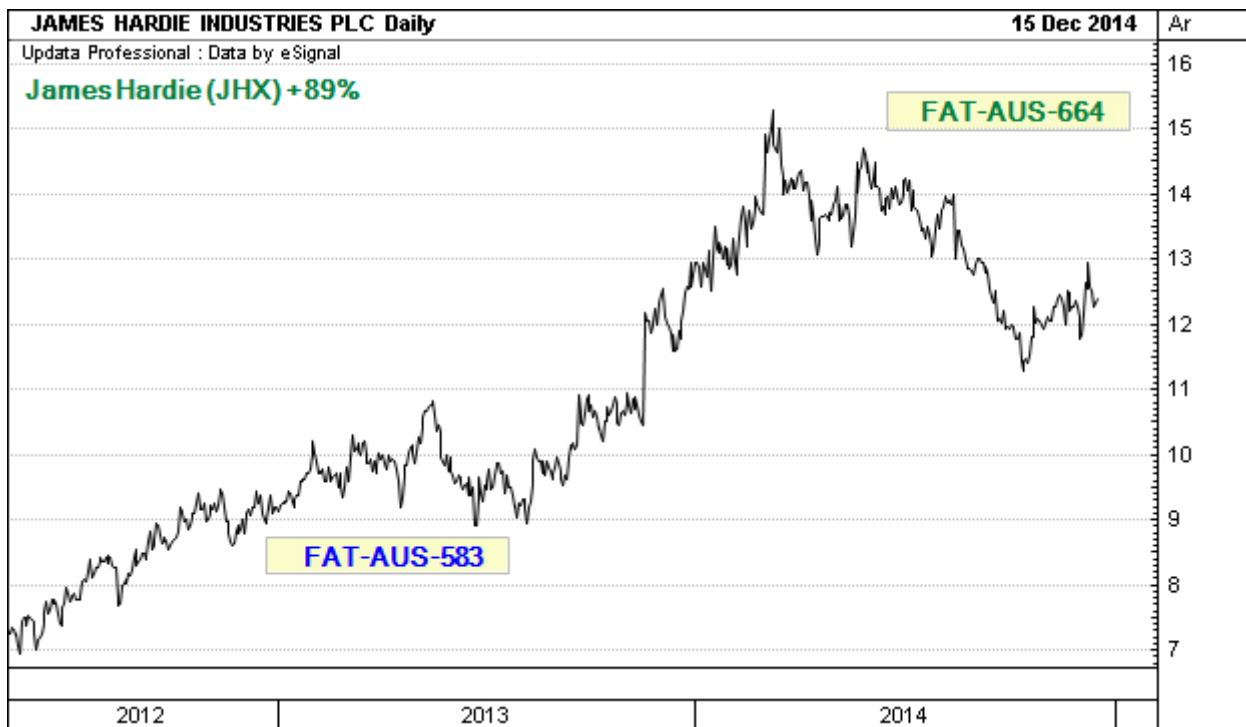
Contrary to our initial expectations when we initiated on Metcash, the deflation and competitive pressures in the domestic supermarket industry have not eased. This was to the detriment of Metcash's independent IGA-retailers and therefore we recommended Members sell their entire position ahead of the company's Strategy Day earlier this year at a price of \$3.15 per share. While this was a relatively disappointing outcome, the significant move south in the interim period suggests it was the right course of action at the time, with the stock closing yesterday's trading at \$1.76.



James Hardie

Fibre-cement maker James Hardie (ASX: JHX) entered the portfolio in July 2007 with an entry price of \$8.05 per share. After a strong performance we recommended Members sell half of their position in March of this year at \$14.68 representing an absolute return including dividends of 89.0 percent and annualised gain of 47.1 percent.

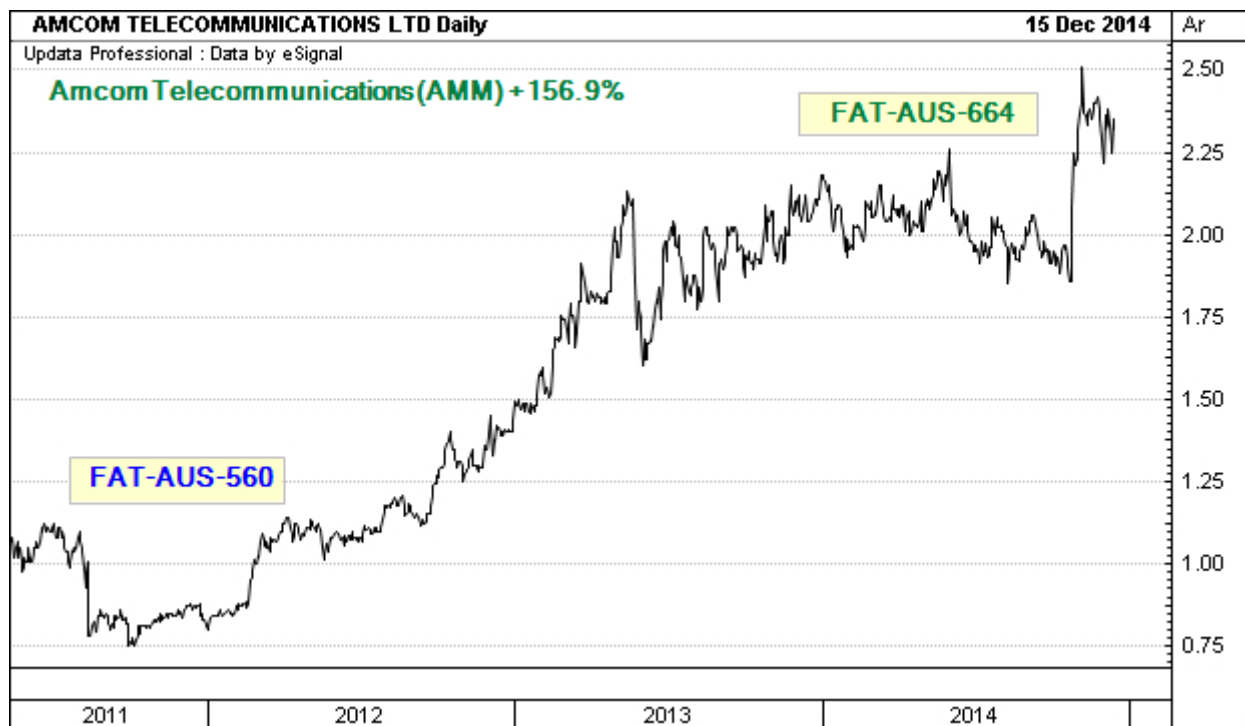
The company was coming off the back of a solid third quarter result, where underlying profit had surged 64 percent, aided by the recovery in the US housing market, leading to volume and price increases that flowed through to operating profit. The stock has since drifted down in trading but we continue to like its leading position in Fibre-cement, a product we believe can continue to pick up market share from more traditional siding products. Therefore we are content to retain our reduced position at this juncture.



Amcom Telecommunications

Amcom Telecommunications (ASX: AMM) has been an admirable performer in the Fat Prophets portfolio since we initiated on the stock in February 2012 at a price of \$0.87 per share. Whilst we continued to view positively the companies outlook in March of this year, the strong performance of the shares and higher price to earnings multiple combined to prompt us to take some additional profits on the stock by recommending Members sell half of their position around \$2.13 per share.

From an absolute basis this represented a return of 156.9 percent (inclusive of dividends) and an annualised gain of 57.0 percent. We note we recommended selling half of Amcom in March 2013 as well. Although Amcom shares drifted south somewhat following our sell half call in March of this year they have come back into favour with the market in recent months. Having lightened our position on two occasions and continuing to have a positive view of the company's growth prospects as well as the possibility of M&A upside we are content to retain our reduced holding.



Coca Cola Amatil

We exited our position in bottler and food processor Coca-Cola Amatil (ASX: CCL) in February at \$11.17 as a range of headwinds of both a temporary and structural nature were clouding the company's outlook. Although our exit price was a little below our entry price of \$11.37 in January of 2011 the dividends received over the holding period kept the position in the black overall with an absolute gain of 15.7 percent and an annualised gain of 4.8 percent.

The decision to exit in February looks to have been justified with the shares being sharply marked down further in April of this year and later reaching a 52-week low of \$8.19 per share. In our view the significant fall in valuation following our exit once again shifted the risk to reward equation for the stock back to favourable. Particularly given signs the worst of the headwinds buffeting the stock look to be abating and other positive changes afoot as a result of a strategic review. Consequently we re-introduced Coca-Cola Amatil to the Fat Prophets portfolio in November at \$9.28 per share.



Boart Longyear

We chose to exit Boart Longyear (ASX: BLY) in February, due to the volatile mining backdrop that had led to a significant deterioration in rig utilisation rates and the severe pricing pressures facing the company. These headwinds had showed no signs of easing in the FY13 results with the company unveiling a large loss.

Furthermore, management’s outlook commentary had provided no light at the end of the tunnel and indeed the share price has continued to fall since our exit at \$0.34 per share (FAT-AUS-662). In retrospect, we were overly reliant on management’s cost and capital reduction strategy to steer the company through the challenging industry conditions—a mistake that proved to be costly as we endured a loss of 77.3 percent (inclusive of dividends), or 42.9 percent annualised.



Blackrock International Gold – C class shares

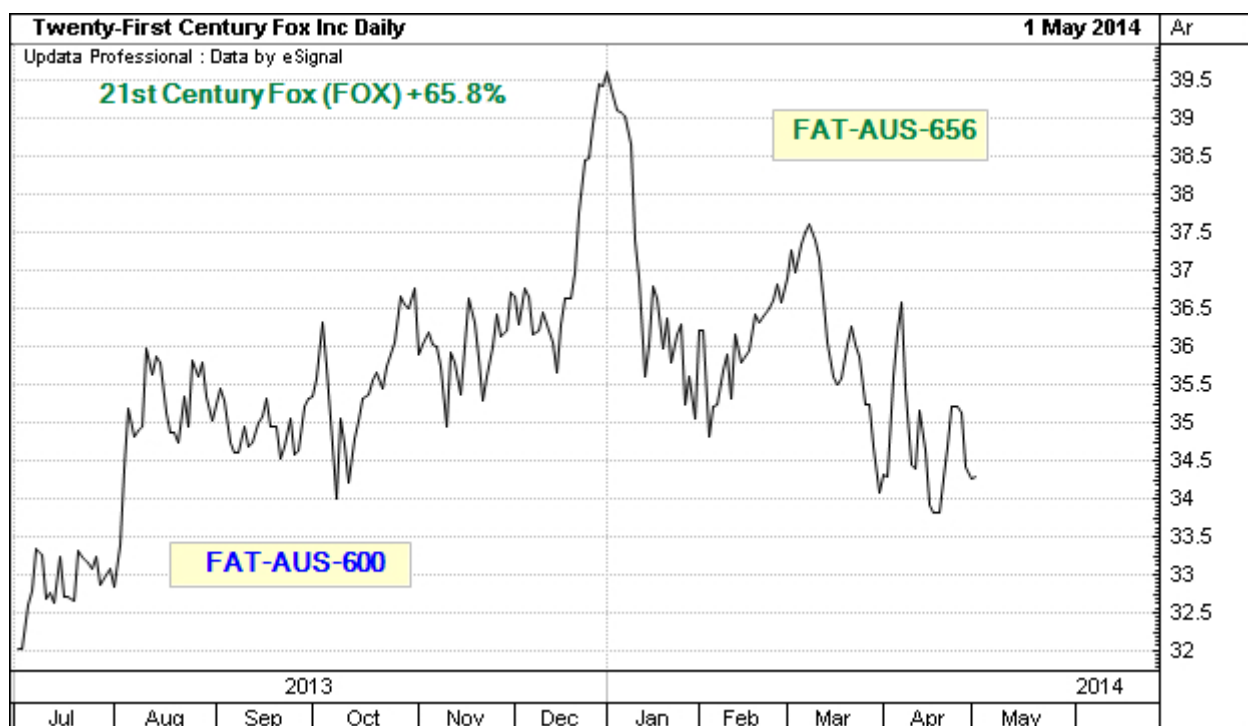
The Blackrock International Gold Fund is a managed fund that we had held in the portfolio since November 2005 (FAT-AUS-255 at \$1.094). The fund actively invests in precious metal producers with an emphasis on gold and positions in some of the largest gold producers. Although we continue to have some exposure to gold miners, the overall weakness in gold saw us pare back our exposure.

The weakness in the gold sector and consequently most producers valuations resulted in our exiting the position in Blackrock International Gold C class shares at a small loss inclusive of distributions of -6.6 percent, or 0.8 percent loss on an annualised basis.

21st Century Fox

The announcement earlier this year by 21st Century Fox (ASX: FOXLV) to begin the share delisting process from the Australian Stock Exchange (ASX) came as no big surprise. Following the demerger implemented in June 2013, the company has very little operating presence 'Down Under'. The company's previous interests in Australian print media assets, pay TV and digital assets are held in the spun-off News Corporation entity (ASX: NWS).

Given the Fat Prophets' Australasian Equities portfolio is primarily focused on ASX-listed stocks, we viewed the delisting proposal as providing the ideal opportunity to crystallise the tremendous gains on the stock since it was first introduced into the portfolio back in November 2012 (FAT-AUS-600) when the stock price was just \$21.56 (split-adjusted). It was our first exit recommendation in 2014.



Certainly, our initial positive investment view on the stock had been vindicated, given the consistent delivery of robust earnings growth, attractive asset mix (particularly Cable Programming) and the strengthening financial position. At the time of our sell recommendation in January of this year at \$35.63, inclusive of dividends, the gain on the position was 65.8 percent since inception and 54.0 percent annualised.

The following stocks are held in the Fat Prophets Concentrated Australian Share Portfolio: AMM, ANZ, BOQ, CBA, JHX

The following stocks are held in the Fat Prophets Income Model Portfolio: AMM, ANZ, BOQ, WBC.

The following stocks are held in the Fat Prophets Small/Mid-cap Model Portfolio: AMM, BOQ

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