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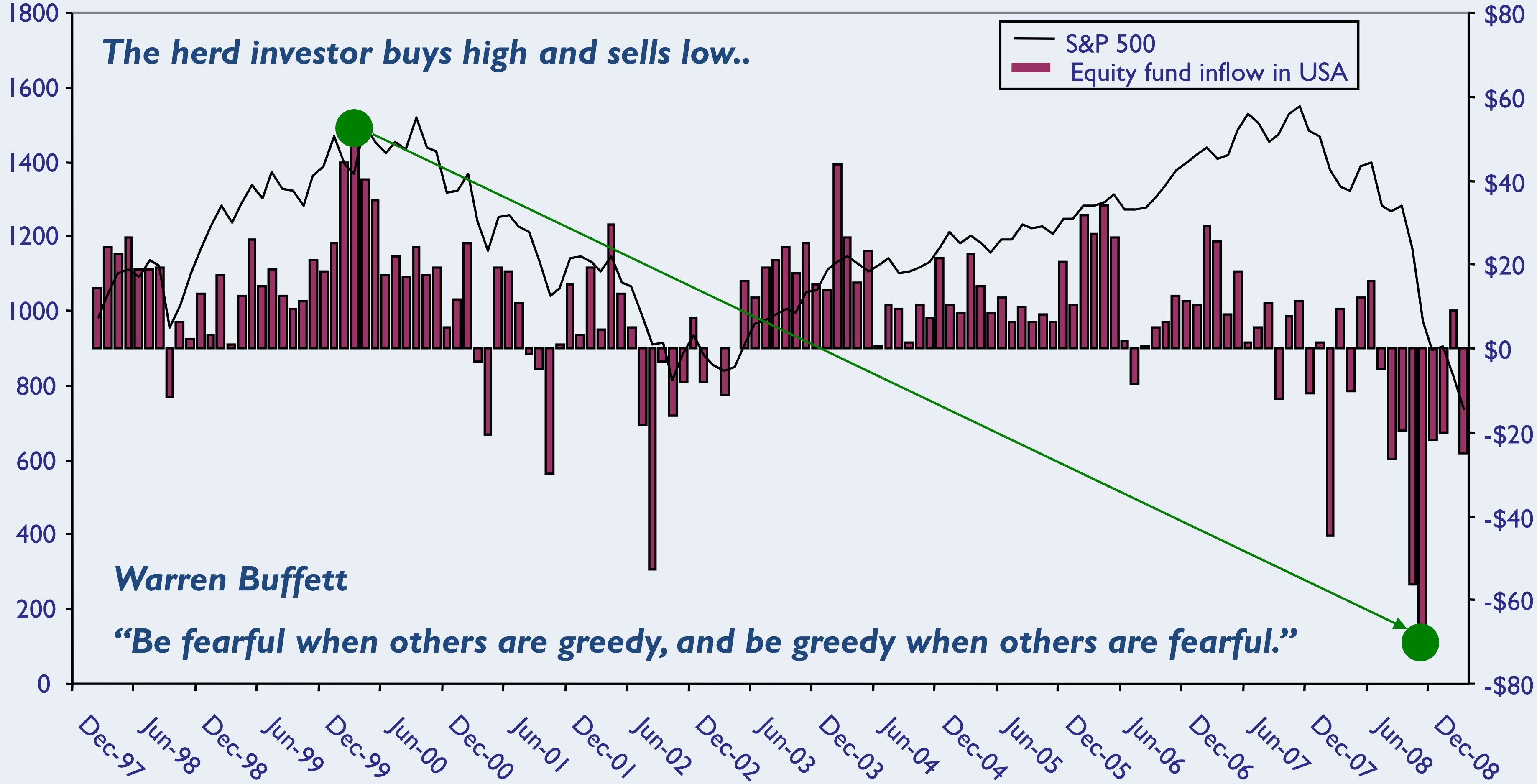
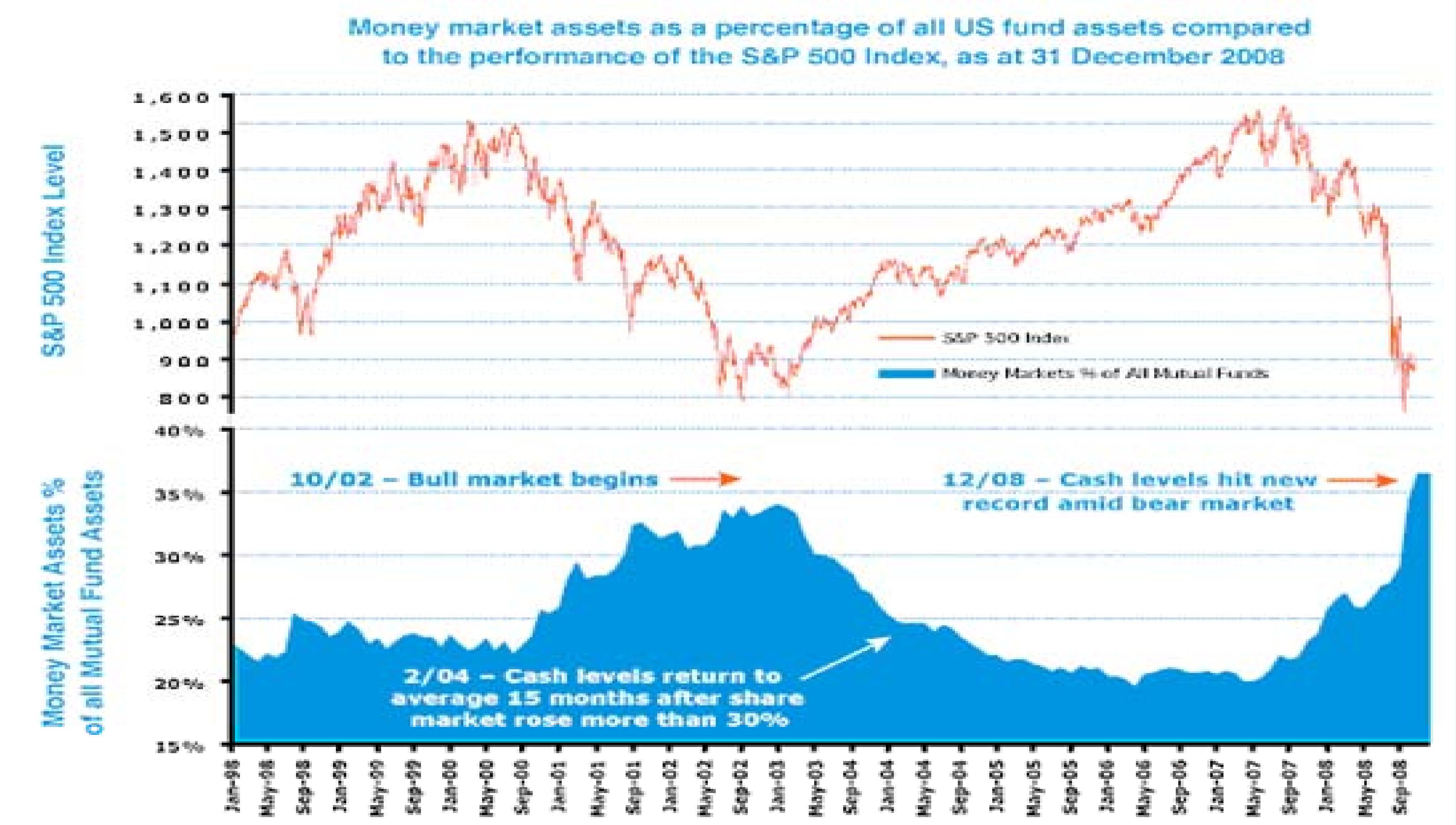
# Equities




Source: ICI (Investment Company Institute)

# Cash




Source: Lexia Nexia, Strategic Insight, FMRCo (MARE) as at 31 December 08

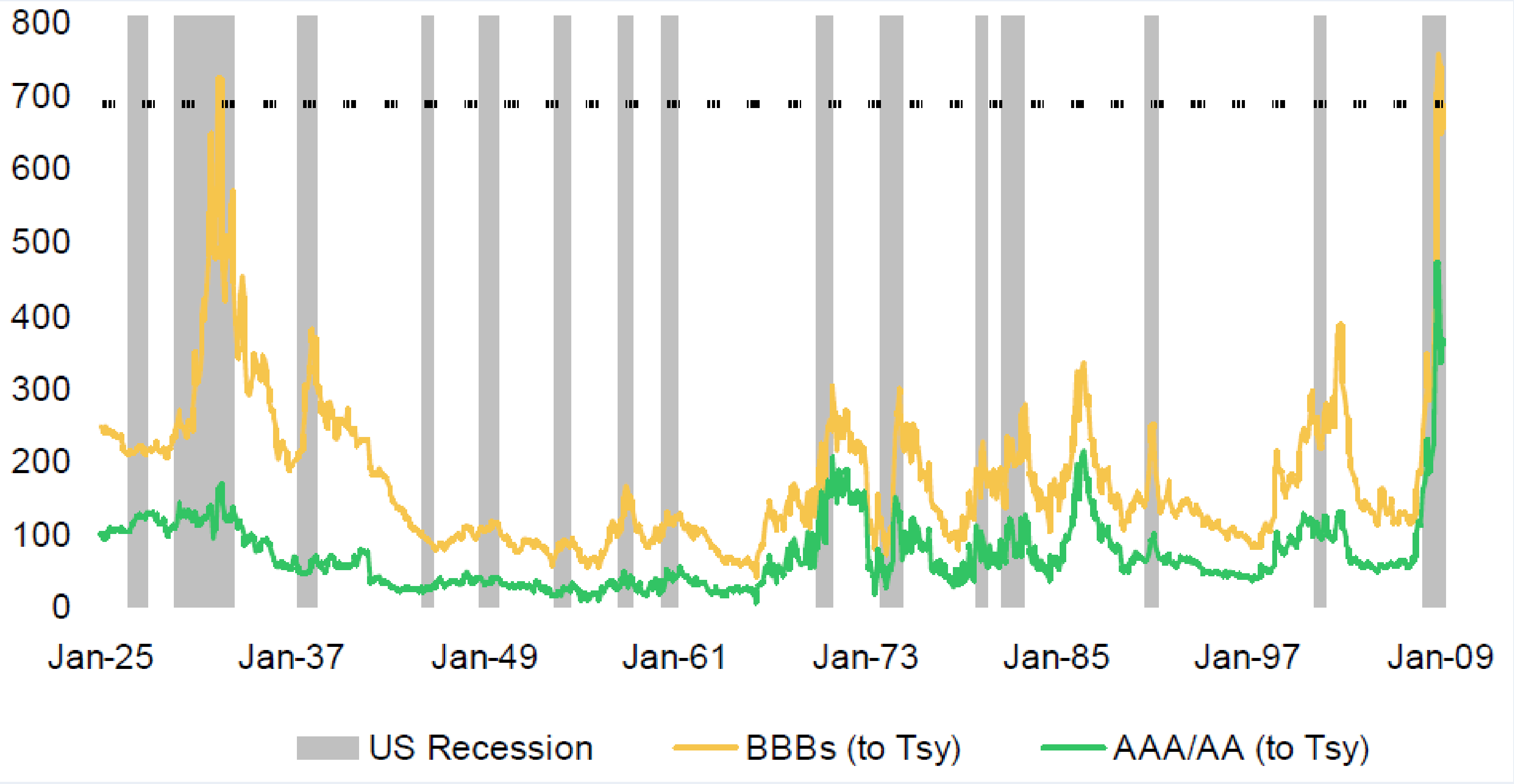
# ING investor presentation

# Visibility

- The best investment opportunities occur when visibility is at its worst
- There has been record selling of shares at bottom decile valuations
- There has been a record build up of cash at record low yields
- We are witnessing the greatest globally co-ordinated stimulus
    - Lower interest rates, plus
    - Record government spending
- Corporations are reducing debt yet investors are demanding record premiums to the yield on government bonds

# Worse than the Great Depression?

Credit Spreads at a Hundred Year Extreme




Source: Moody's, Yield Book, NBER, Morgan Stanley Research

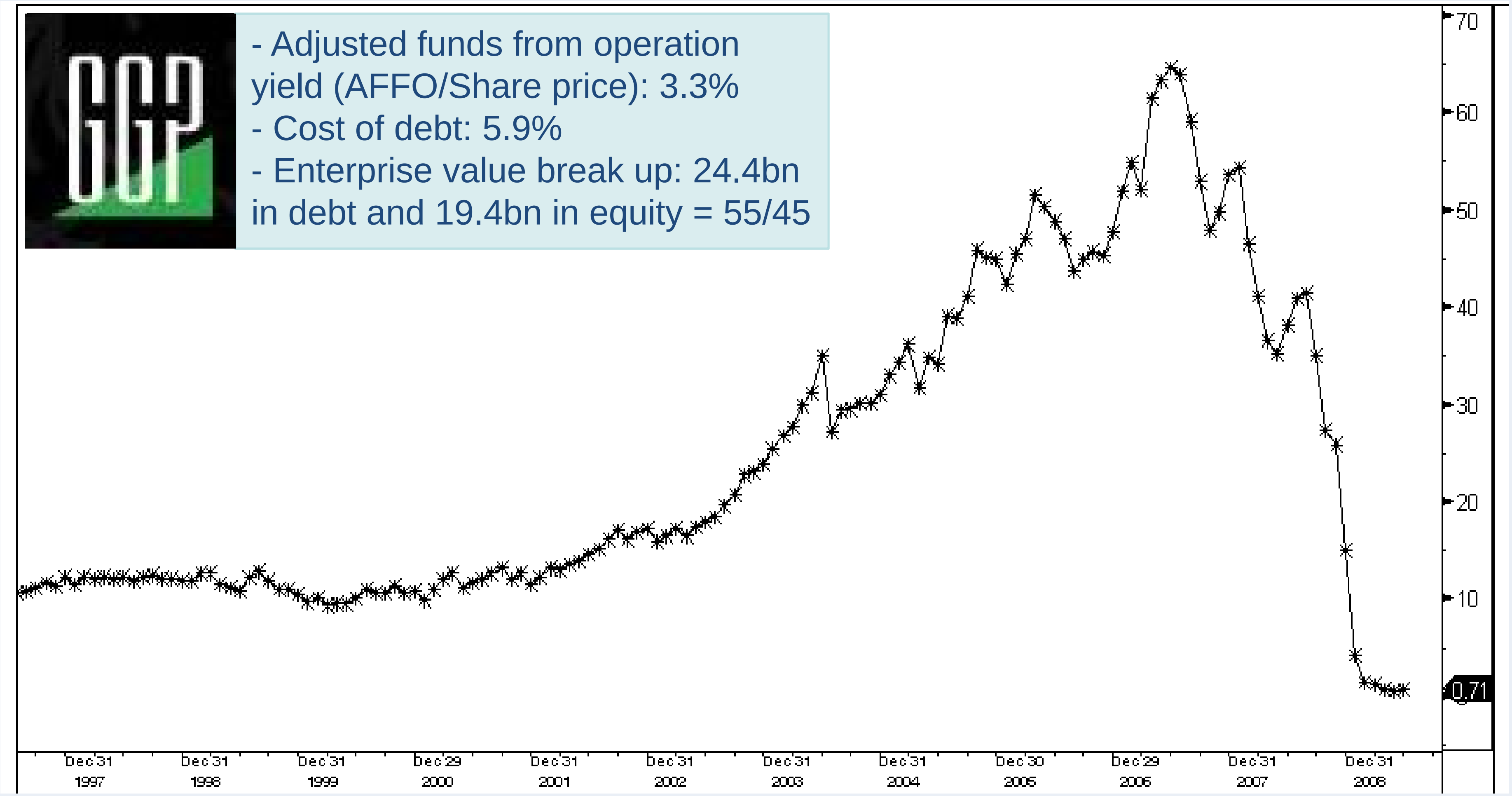
# Yield curve

| Issuer | Yield |
|---|---|
| Term deposit - major bank (1 year) | 2.90% |
| Government guaranteed - major bank senior debt (3 years) | 3.75% |
| Non-government guaranteed - major bank senior debt (3 years) | 4.40% |
| BHP | 6.60% |
| Tabcorp | 6.85% |
| Non-government guaranteed - major bank sub debt (3 years) | 8.10% |
| Rio Tinto | 10.60% |
| Morgan Stanley | 11.00% |
| Orica | 17.00% |

# Anomalies

- Government debt vs. government guaranteed debt
- Subordinated debt vs. hybrid securities
- Onshore vs. offshore

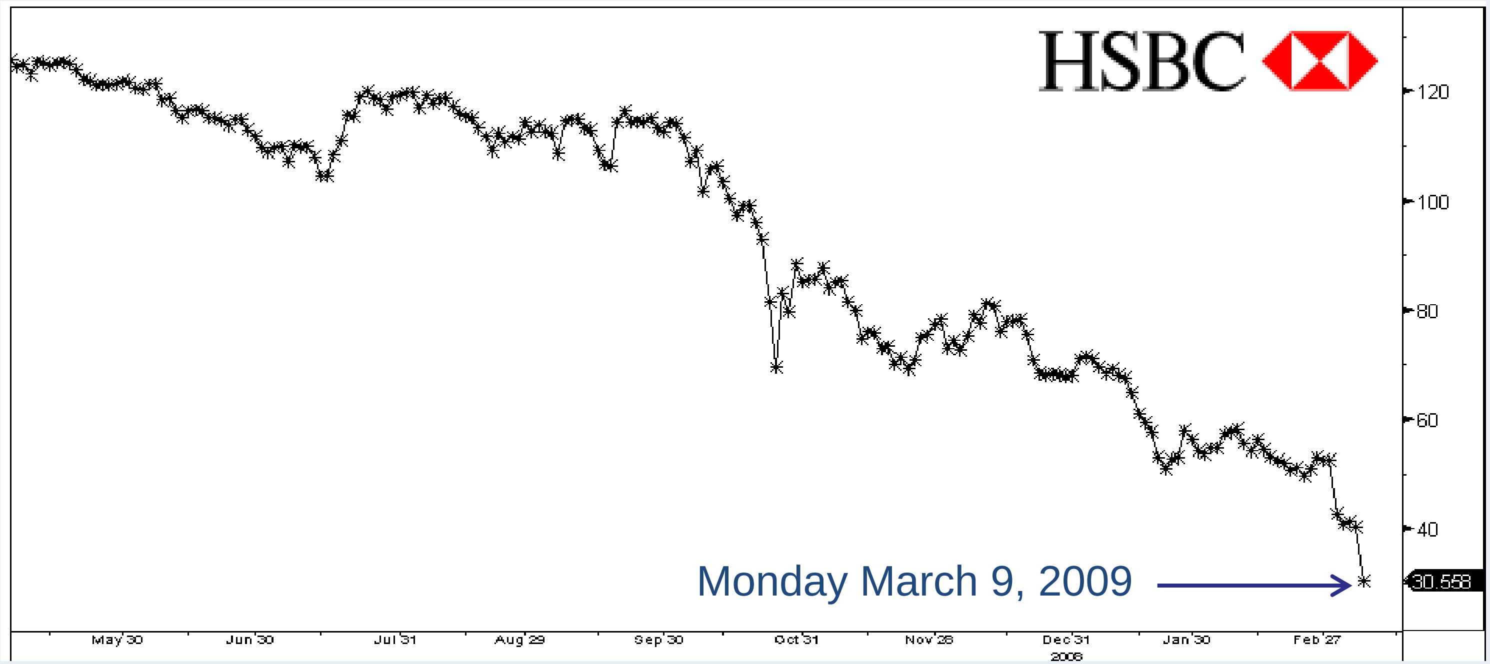
# General Growth Property



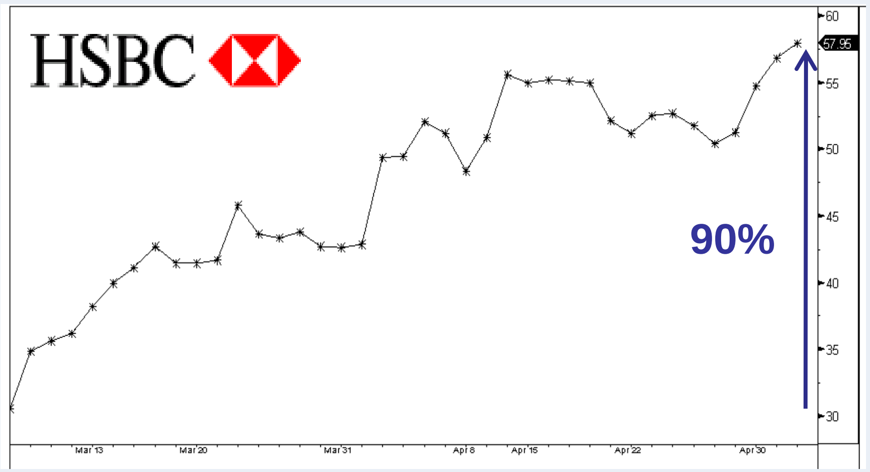
# HSBC plunge brings commentator to tears

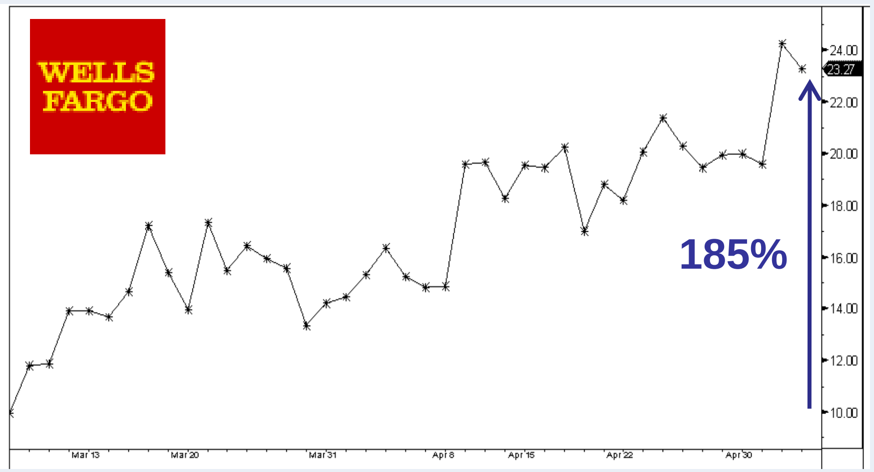
**(Monday March 9, 2009)**

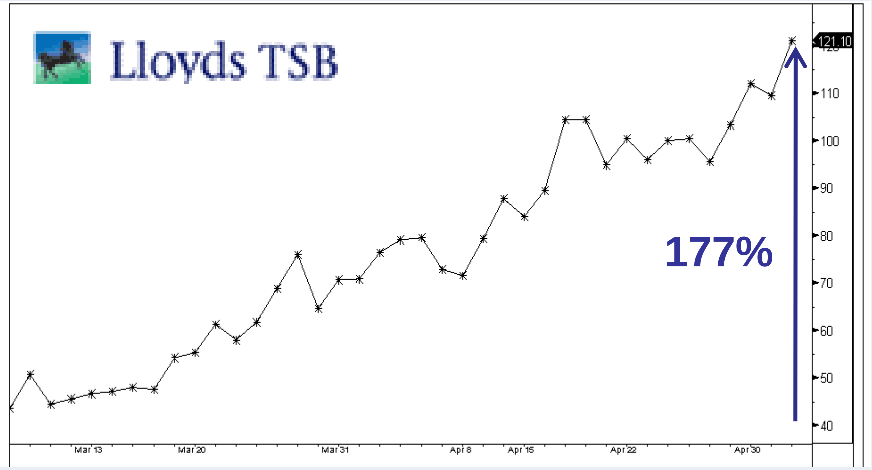
A veteran Hong Kong stock commentator burst into tears during a live television broadcast as she saw HSBC's shares plunge dramatically, seconds before the end of Monday's trading. Agnes Wu's comments on the recent volatility of the banking giant's Hong Kong-listed shares trailed off as she saw its price slump to 33 Hong Kong dollars ($US4.23) after a last-minute sell order, a clip on Cable News showed.

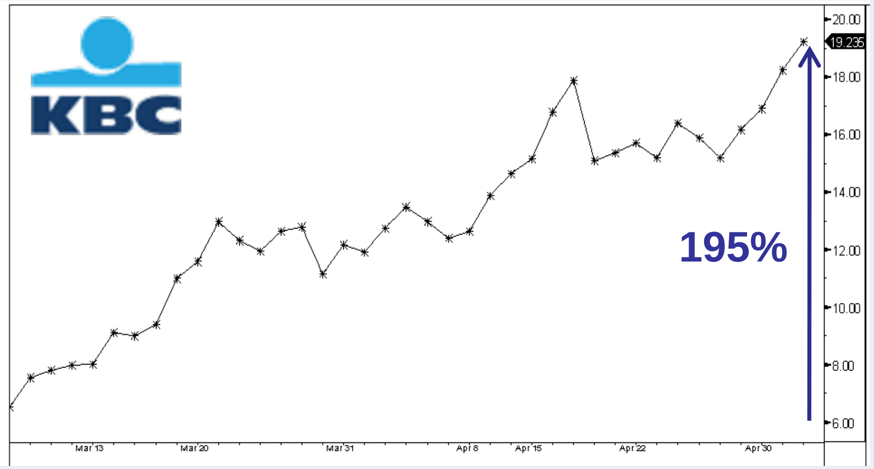


# It is always darkest just before dawn



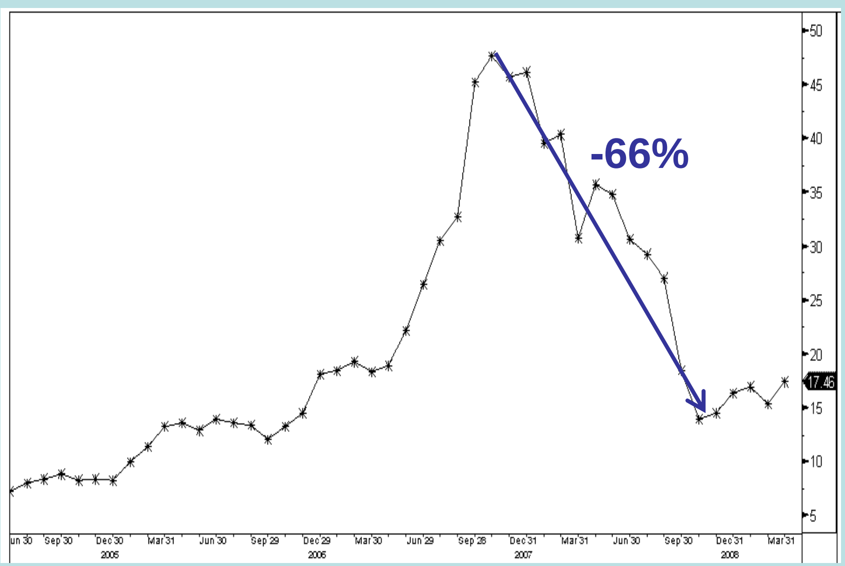




Source: Bloomberg as at 5 May 2009

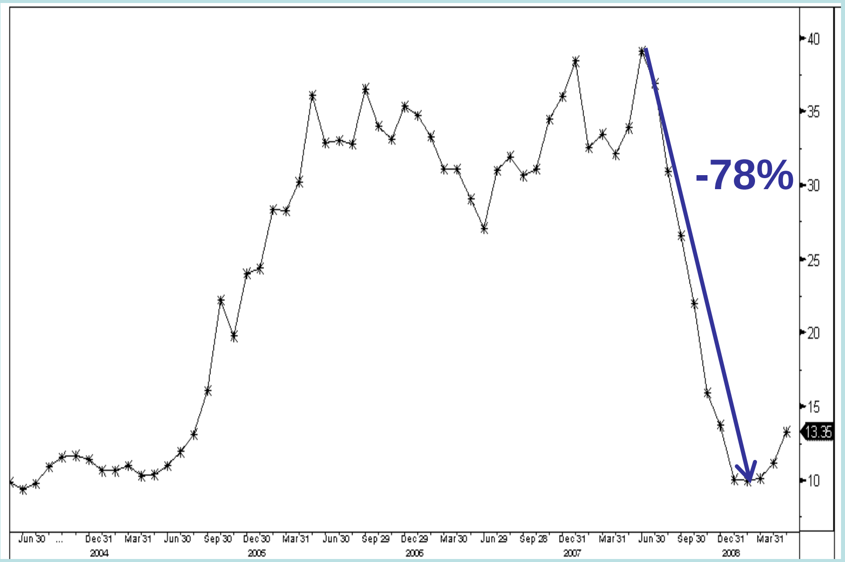
# China Shenhua Energy




- ➢ Worlds second largest producer of thermal coal
- ➢ A low cost producer due to size and quality of ore body
- ➢ Owns rail / port infrastructure: another cost advantage
- ➢ Minimal debt
- ➢ 90% of output sold on long-term contracts to domestic power companies
- ➢ Future Chinese demand for coal is undeniable

Source: Bloomberg

# Gazprom




- Long life low cost gas reserves
- Supplies 30% of Europe's gas needs
- Opportunity provided by falling gas prices and collapse of Rouble following Georgian War
- Purchased on 3x earnings with depressed gas prices

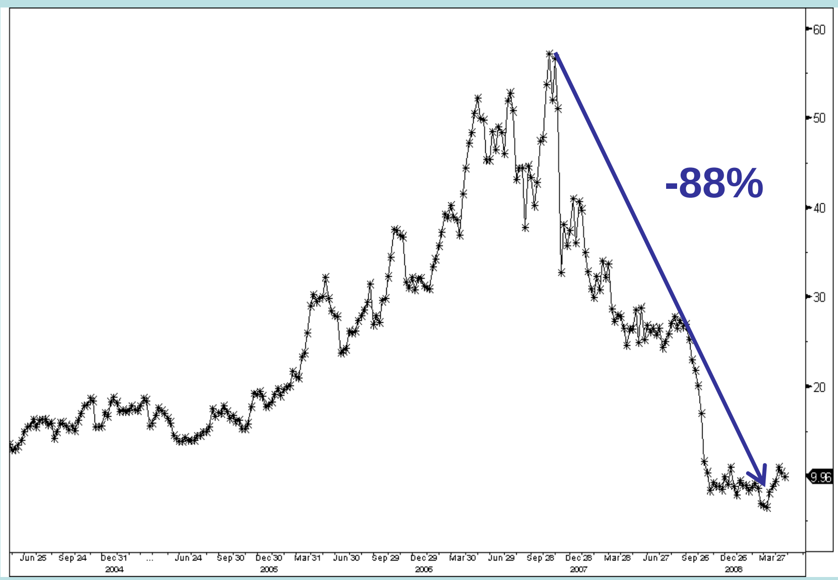
Source: Bloomberg

# Google


- Global brand, the dominant business model in new media
- Structural growth of online
- Limited capital employed - $6.3B vs $8B EBIT
- Net cash on balance sheet
- 50%+ operating margins
- Purchased on 15* earnings

Source: Bloomberg

# Sotheby's




- Global duopoly on art auction market
- Share price decimated as art market dried up and commission earnings followed
- Purchased at book value – New York HQ plus works of art
- Commission business and brand effectively purchased for free
- At some point the art market will recover and Sotheby's will remain a key place to trade

Source: Bloomberg

# Banks ?

# Conclusion

- Safety in numbers does not work in the investment world
- The investment world has gone from under pricing risk to over pricing it
- Yield securities in February represented a once in a lifetime opportunity
- Equities, likewise were compelling
- When everyone believes that cash is king, cash is more likely to be trash

# Investment Presentation - Disclaimer Statement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# Appendix 1: Warren Buffett on Wells Fargo

**'Banking is a very good business unless you do dumb things,' says Wells Fargo's largest shareholder.**
Interview by Adam Lashinsky

SAN FRANCISCO (Fortune) -- As the largest shareholder of Wells Fargo through Berkshire Hathaway, Warren Buffett knows the San Francisco bank deeply. He first invested before Wells Fargo was bought by Norwest, where current Wells Chairman Dick Kovacevich was CEO. As part of his reporting for his feature on Wells Fargo, Fortune Editor at Large Adam Lashinsky spoke at length with Buffett by telephone on March 26.

**Fortune: How is Wells Fargo unique?**

Warren Buffett: It's sort of hard to imagine a business that large being unique. You'd think they'd need to be like any other bank by the time they got to that size. Those guys have gone their own way. That doesn't mean that everything they've done has been right. But they've never felt compelled to do anything because other banks were doing it, and that's how banks get in trouble, when they say, "Everybody else is doing it, why shouldn't I?"

**What about all the smart analysts who think no big bank can survive in its present form, including Wells Fargo?**

Almost 20 years ago they were saying the same thing. In the end banking is a very good business unless you do dumb things. You get your money extraordinarily cheap and you don't have to do dumb things. But periodically banks do it, and they do it as a flock, like international loans in the 80s. You don't have to be a rocket scientist when your raw material cost is less than 1-1/2%. So I know that you can have a model that works fine and Wells has come closer to doing that right than any other big bank by some margin. They get their money cheaper than anybody else. We're the low-cost producer at Geico in auto insurance among big companies. And when you're the low-cost producer - whether it's copper, or in banking - it's huge.

Then on top of that, they're smart on the asset side. They stayed out of most of the big trouble areas. Now, even if you're getting 20% down payments on houses, if the other guy did enough dumb things, the house prices can fall to where you get hurt some. But they were not out there doing option ARMs and all these crazy things. They're going to have plenty of credit losses. But they will have, after a couple of quarters of getting Wachovia the way they want it, $40 billion of pre-provision income.

And they do not have all kinds of time bombs around. Wells will lose some money. There's no question about that. And they'll lose more than the normal amount of money. Now, if they were getting their money at a percentage point higher, that would be $10 billion of difference there. But they've got the secret to both growth, low-cost deposits and a lot of ancillary income coming in from their customer base.

**Insurance revenues for example, which had double-digit revenue growth in 2008**.

And I would say that most of the critics of Wells don't even know they've got that business. That business alone is worth many billions of dollars. And their mortgage business, as you can imagine in this period, I mean, the volume that is poring through there, is huge. The critics have been right on other big banks, so I think they're inclined to sweep Wells in as well to some extent. And if you've been right on Citi and

# Warren Buffett on Wells Fargo

you've been right on BofA, it gets easy to say, well, they're all going to go.

We own stock in four banks: USB, Wells, M&T, and SunTrust. SunTrust I don't know about because South Florida is going to be the last to come back, and they've got a concentration down there. The other three, they're going to have a lousy year, but they'll come out of it with far more earnings power. The deposits are flowing in. The spreads are wide. It's a helluva good business.

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**Dick Kovacevich specifically told me to ask you your views on tangible common equity**.

What I pay attention to is earning power. Coca-Cola has no tangible common equity. But they've got huge earning power. And Wells ... you can't take away Wells' customer base. It grows quarter by quarter. And what you make money off of is customers. And you make money on customers by having a helluva spread on assets and not doing anything really dumb. And that's what they do.

Incidentally, they won't lend Berkshire money. They're not interested in national credits or any of that stuff where the spreads are narrow. We did a big deal about six or seven years ago on Finova, which we did jointly with Leucadia. And what was then the old First National of Boston sort of headed the deal up, and people would come in for $500 million or $200 million. Wells wasn't interested. There wasn't enough money in it, basically. I got a big kick out of that because that was exactly how they should think. Everybody else wanted to be in it, and they were doing it for 20 basis points or something of the sort.

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# Warren Buffett on Wells Fargo

And they'd make commitments for all kinds of credit for 6 or 8 basis points, and the ones that were in the underwriting business, they would do it just get the underwriting.

**But back to tangible common equity...**

You don't make money on tangible common equity. You make money on the funds that people give you and the difference between the cost of those funds and what you lend them out on. And that's where people get all mixed up incidentally on things like the TARP. They say, 'Well, where'd the 5 billion go or where'd the 10 billion go that was put in?' That isn't what you make money on. You make money on that deposit base of $800 billion that they've got now. And that deposit base I guarantee you will cost Wells a lot less than it cost Wachovia. And they'll put out the money differently.

They'll have to work through a lot of this stuff that they inherited from Wachovia. Those option ARMs, they explained exactly how they break them down, and in the end they may lose 3 or 4 billion more. Nobody knows exactly. But I would say that California residential real estate is not deteriorating. It hasn't moved up. But it has flattened out with good volume recently. So my guess is that the option ARMs will work out about as they guessed.

**What if the Treasury imposes new capital requirements? Will it hamper their earnings power?**

I don't think it'll hamper their earnings. But if you make them sell a lot of common equity it would kill the common shareholder. It wouldn't increase the earning power in the future, and it would increase the shares outstanding. Wells, if they want another $10 billion in common equity or something like that in Wells, they'll have it in a very short period of time at this dividend rate. [In March, Wells cut its dividend by 85%.] Wells will be piling up the equity while they're paying nominal dividends. They could afford to pay the old dividend. But since they won't be paying the old dividend, that's $4 billion a year or something that they'll be adding to equity.

I would have been fine if they had just said, 'Look it, we'll quit paying any common dividend until our equity has gone up by whatever it might be, 10 or 15 billion.' And they'd get there in no time. Then they could pay the regular dividend. They elected to do it this other way because everybody seems to be kind of doing it. The idea of forgoing all or most of the dividend for a year to build the common equity ratio up, if that's what the government wants, that's fine. But that isn't really the key to the future of Wells, unless the regulators make it the key to the future of Wells. The key to the future of Wells is of the sort. And they'd make commitments for all kinds of credit for 6 or 8 basis points, and the ones that were in the underwriting business, they would do it just get the underwriting.

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**How is Wells differentiated from the banks you own and the ones you don't?**

Wells just has a whole different attitude. That's why Kovacevich calls them retail stores. He doesn't even like the word banking. I mean, he is looking to have a maximum enduring relationship with many, many millions of people. Tens of millions. And at the base of it involves getting money in very cheap. When you do that that's a helluva start in the business. The difference between getting your money at 1-1/2 % and 2-1/2% on a trillion-dollar asset base is $10 billion a year. It's hard to overemphasize that. He thinks more like Sam Walton than he thinks like J.P. Morgan. I'm talking about the individual there. He's a retailer. He's not trying to influence Washington or be the most important guy on the scene or anything like that. He's just trying to do business with millions of people every day and make a few bucks off of them.

**Now that you mention it, Kovacevich has done a pretty good job of annoying Washington, wouldn't you say?**

That's hard to tell. There's an advantage to being that way too. He's not going to cozy up or be sycophantic toward his regulator, and I would say most bankers probably are now. They need to be. But his strong point is retailing not diplomacy. I kind of like that. It's hard for a guy that knows his institution forward and backwards to have somebody come in that really

# Warren Buffett on Wells Fargo

may be working off a check list or something and is telling him what to do. And I'm sure that Dick gets antagonized by that sometimes. In the end, he's got the record. And he's got the business to back up what he's doing. To the extent that his tangible common equity is low, a) nobody was even talking about that a year ago. And b) they should be talking about earning power. But it comes about in part because he saved the FDIC's bacon on Wachovia. I mean they had a deal on Citigroup that had big assistance involved in it, and the FDIC moved about what would have been about 5% of the deposits in the United States without a dime of expense to the taxpayer or the FDIC to Wells. And Wells took it over. And if they'd gone to Citigroup a) they would have looked like idiots, and within a very short period considering what happened to Citi. So to penalize them because they solved the FDIC's problem without cost to the FDIC would be a little crazy. And I imagine that's what gets Dick a little riled up.

**So what is your metric for valuing a bank**

It's earnings on assets, as long as they're being achieved in a conservative way. But you can't say earnings on assets, because you'll get some guy who's taking all kinds of risks and will look terrific for a while. And you can have off-balance sheet stuff that contributes to earnings but doesn't show up in the assets denominator. So it has to be an intelligent view of the quality of the earnings on assets as well as the quantity of the earnings on assets. But if you're doing it in a sound way, that's what I look at.

**How confident will you be in Wells when Kovacevich retires?**

Well, John [Stumpf] is in charge. Dick is a terrific help to John. I play bridge with John on the Internet. He plays under the name of HTUR. His wife's name is Ruth. My bridge partner, who I probably play bridge with four times a week, developed online banking for Wells. A woman named Sharon Osberg. And she's worked with those people. And she told me about John Stumpf ten years ago. I've had some insight through her on these people. But the real insight you get about a banker is how they bank. You've got to see what they do and what they don't do. Their speeches don't make any difference. It's what they do and what they don't do. And what Wells didn't do is what defines their greatness.

**How is John's bridge game?**

John is a very good bridge player. But he doesn't play as much as I do. I play all the time. He's smart. He's a different personality than Dick. Dick is a real sales person. They both subscribe to the same principles of banking. They just don't think you have to do things that the other guy is doing.

# Appendix 2: Zebra

**Extracts taken from 'The New Money Masters' By John Train:**
**Acorn Fund Report - Ralph Wanger**

"Zebras have the same problem as institutional portfolio managers. First, both seek profits. For portfolio managers, above average performance; for zebras, fresh grass.

Secondly, both dislike risk. Portfolio managers can get fired; zebras can get eaten by lions.

Third, both move in herds. They look alike, think alike and stick close together.

If you are a zebra and live in a herd, the key decision you have to make is where to stand in relation to the rest of the herd. When you think that conditions are safe, the outside of the herd is the best, for there the grass is fresh, while those in the middle see only grass which is half-eaten or trampled down. The aggressive zebras, on the outside of the herd eat much better.

On the other hand - or other hoof - there comes a time when lions approach. The outside zebras end up as lion lunch, and the skinny zebras in the middle of the pack may eat less but they are still alive.

A portfolio manager for an institution such as a bank trust department cannot afford to be an Outside Zebra. For him, the optimal strategy is simple; stay in the centre of the herd at all times. As long as he continues to buy the popular stocks... he cannot be faulted. To quote one portfolio manager. "It really doesn't matter a lot to me what happens to Johnson & Johnson as long as everyone has it and we all go down together". But on the other hand, he cannot afford to try for large gains on unfamiliar stocks that would leave him open to criticism if the idea fails".

Needless to say, this Inside Zebra philosophy doesn't appeal to us as long-term investors.

We have tried to be Outside Zebras most of the time, and there are plenty of claw marks on us to prove it