Mosaic Special Situations Fund

January 2012

The Mosaic Special Situations Fund underperformed during the month of January, increasing by 0.9% compared to the S&P/ASX All Ordinaries Accumulation Index's dynamic 5.2% start to the New Year.

Photon Group announced, as widely expected, that current Australian agencies boss Matthew Melhuish will be appointed new chief executive officer, and a review of corporate overheads should see costs slashed by $4 million to reflect the smaller size of the company.

Whilst this was positive news, the 31 December half year trading was disappointing. Photon also continued its practice of making unusual 'pro-forma' comparisons with the prior year, this time excluding the contribution of one of its largest clients, Telstra, from the comparison. Given that the Telstra contract was lost, rather than sold, it is the Manager's preference that it be included in prior year comparisons.

With the Telstra results included, pro-forma EBITDA was down substantially more than the 7.5% indicated. Better results are needed to make a successful investment case from here and Photon closed down 5.7% for the month.

QBE Insurance indicated that its earnings would decline 40% to 50% in 2011 due to record levels of catastrophe claims. The stock price was promptly thumped by the market, dropping 21% immediately after the announcement. Insurance is a volatile business, and QBE wasn't the only one suffering; **Suncorp Group** announced natural hazard costs $120m higher than provisioned and **Calliden Group** reported a full year loss due to the 'continuation of unprecedented catastrophe activity'. **Insurance Australia Group** affirmed its financial year 2012 guidance on 26 October on the assumption that 'losses from natural perils are in line with budgeted allowances', but then announced in the New Year that first-half losses are anticipated to be in the range of $400m - $420m, compared to allowances of $266m.

Performance Data as at	31/01/2012
1 month	0.88%
3 months	-0.61%
6 months	-2.12%
1 year	9.53%
2 years (p.a.)	5.11%
3 years (p.a.)	27.60%
5 years (p.a.)	-0.28%
Since Inception (p.a.)*	2.67%
Net Asset Value ($)	0.9435
Fund Size ($ million)	34.86

* Inception date of Fund 30/09/2004

Top 10 Portfolio Holdings	%
Oceania Capital Partners Ltd.	29.71%
QBE Insurance Group Ltd	11.04%
Infigen Energy	9.28%
Photon Group Limited	6.85%
UXC Limited	6.03%
ING Real Estate Community Living	5.76%
Cash	4.86%
1300 Smiles Limited	4.79%
Reckson New York Property Trust	4.09%
Watpac Limited	3.53%
Other holdings	14.08%
TOTAL	100.00%

The whole industry is currently reviewing its pricing for catastrophe businesses, and the Manager is confident that QBE CEO Frank O'Halloran and his senior executives have QBE headed in the right direction. The Manager took the opportunity to add to the Fund's QBE position at very attractive prices.

After ignoring the very positive news released late in December, investors looked favourably on **ING Real Estate Community Living Group (ILF)** during January, sending the price up 12.5% on mounting speculation that a sale of its New York assets is imminent. The gap between price and value has narrowed somewhat but the Manager thinks that the stock still looks cheap.

In early February **Oceania Capital Partners (OCP)** announced the completion of its off market buy-back. OCP received applications slightly in excess of the maximum buy-back pool, which resulted in a scale back of 3%. The Manager tendered all the Fund's OCP shares through the buy-back and as a result the Fund's position in OCP as of early February has now been reduced to less than 1%. As previously indicated the Manager views the buy-back as a sensible result for all shareholders, and is looking forward to investing the proceeds from OCP in new opportunities.