KING TIDE ASSET MANAGEMENT

QUARTERLY REPORT

	King Tide	Blended Benchmark*
Quarter NZDs	0.76%	3.26%
Quarter AUDs	4.34%	7.34%
Year to Date NZDs	0.76%	3.26%
Year to Date AUDs	4.34%	7.34%

At the end of the quarter, KT had nine managers, with allocations ranging between 6.0% and 16.1%. Allocation changes have been predominately performance driven.

Underlying managers have been growing and now manage just over NZ$2.2bn. However, this is skewed by one manager who manages NZ$1.25bn. The average size of the other eight funds is NZ$113m, ranging between $27m and $190m.

Three managers outperformed the blended benchmark. The two NZ managers who actively manage back to NZ dollars had a currency advantage, but also had very good quarters, gaining 23% and 9%. One Australian based fund was up 15% in NZDs, 19% in Australian dollars. These three funds make up 30% of the King Tide fund.

Our two worst performing managers run very different styles, but came in well below the market with draw downs of around 2% in AUDs, which translated into falls of 6% in NZDs. They comprise 25.2% of the portfolio.

The four other funds made between 1% and 5% in AUDs.

We don't have a strong view on the direction of the NZ/AUD cross and even if we did, it would make no difference to our management of the fund. King Tide currently offers only NZ dollar units, so the KT fund should be viewed as 80% AUD and 20% NZD currency exposure.

The Australian market as measured by the ASX200 index made the bulk of its gains in January, rising 5.08%. February and March were positive but by less than 1%. The NZX50 was the reverse, with gains of less than 1% in January and February, but a 5.63% rise in March.

Two of our managers have now closed to new money, but will allow existing investors (King Tide being one of them) to add. A third manager has indicated that they will be hard closing in the next couple of months, which means even existing investors cannot add.

This illustrates an important difference between our managers and other funds. Our managers are focused on performance, not size. They are investors, not money gatherers. Their incentives are aligned with those of their investors. They stand to make far more money for themselves through performance fees, than through fixed management fees. And of course each of them has the bulk of their own net worth invested in their funds, which again focuses them on performance rather than size.

While we would have preferred our first quarter to be well ahead of markets, our ultimate goal is not to chase relative returns, but positive returns. Rob Campbell, our Chairman, refers to this in his covering letter attached. We are pleased therefore to report a first quarter of positive returns. There will be quarters when this will not be the case, if historical patterns are anything to go by.

I also attach a "Comment on Risk" which Rob has compiled to give you an idea of how we think about risk at King Tide. This will be available on our web-site.

One cost which will not be present in future quarters is the initial buy/sell spread of underlying managers. This resulted in about -0.44% lower return in the quarter. There was also a currency loss of -0.22% between funds invested at the end of December and funds remitted to managers at the beginning of January. The actual performance of the managers outside of these one-off affects, but after management fees, was 1.38%.

How are our managers seeing things?

Here are excerpts from manager reports to give you insight into their thinking:

“As we stand contemplating the next financial year the current uncertainty might see more changes to the portfolio. Building and retail are weak as is any discretionary corporate spending on areas like IT etc. We get the sense that many domestically oriented Australian companies are giving up on a recovery and instigating further restructuring initiatives despite significant streamlining post the first bout of the GFC. Mining service companies and occasional private equity targets have been the only game in town. We struggle to see much value in most of these but we have rarely seen corporate Australia, its fund managers and brokers so depressed. It is not a sufficient condition for a market bottom but it is certainly a necessary one.”

“Equity markets remain very difficult to read, in our view. There is a curious yet frustrating randomness in the behavior of the Australian stock market. Its correlation to international markets has declined and daily stock and sector moves have become increasingly unpredictable. We think this reflects a persistent earnings downgrade cycle, growing concerns about China’s growth trajectory and heightened political uncertainty.”

“The Australian market has lagged markets in the US, Asia and parts of Europe so far this year due to a strong Australian dollar and a deterioration in domestic economic indicators that is making investors question earnings forecasts once again. The RBA is now signaling in its latest minutes that monetary easing could be entertained as early as May and this, together with weakness in the Australian dollar, could be the trigger for Australian equities to begin to catch up to global equities over the remainder of the year. Consequently we remain cautiously optimistic regarding the direction of Australian equities with valuations remaining below long-term averages. We expect an increase in the frequency of earnings updates over the next two to three months to provide catalysts for both long and short positions.”

Two managers have highlighted Transpacific Industries as an undervalued company. Here's how one manager sees it:

TPI is a **waste management and recycling** company, dealing with residential, construction, medical and hazardous waste. It also owns a specialised fleet of vehicles that manage the waste disposal

•After a series of acquisitions in 2005-2007 **funded by debt**, the TPI **balance sheet was heavily stretched** and it experienced financial stress and a recapitalisation during the GFC

•Nevertheless, due to its relatively low sensitivity to the economy, TPI continued to deliver a **high quality low cyclical income stream** from businesses integral to the Australian economy

•With **new management** in place and another capital raising, TPI is now investment grade again. At its current price, TPI is trading on a **2013 free cashflow yield of 11%**, an outstanding return for a relatively low level of risk

In the quarter I visited all of our managers in Australia, and visited two others which we are looking at. I also learned of a relatively new fund launched last year, which we have added to our short list. It is likely we will add a new manager at the end of May.

We are extremely grateful to those of you who have invested alongside ourselves, and look forward to a long and mutually beneficial partnership.

Sincerely,

Mark Houghton
CEO