Companies Index	
Aristocrat	2
AVV Limited	2
SAI Global	2
Patrick Corp	2
Petsec Energy	2
Cochlear	3
STW Group	3
Ten Network	3

WELCOME to the second quarterly report of Selector Funds Management Limited (SFM). The SFM model portfolio (SFM_{MP}) was started in January 2003. Our reporting tables are based on an investment of $1.0M with SFM. The value of **$1,000,000** invested in Jan 2003 is **$1,189,307** an absolute return of **18.93 %** for the 4 quarters or 12 months to December 31 2003, shown below against the All Ordinaries Accumulation Index (AOAI).

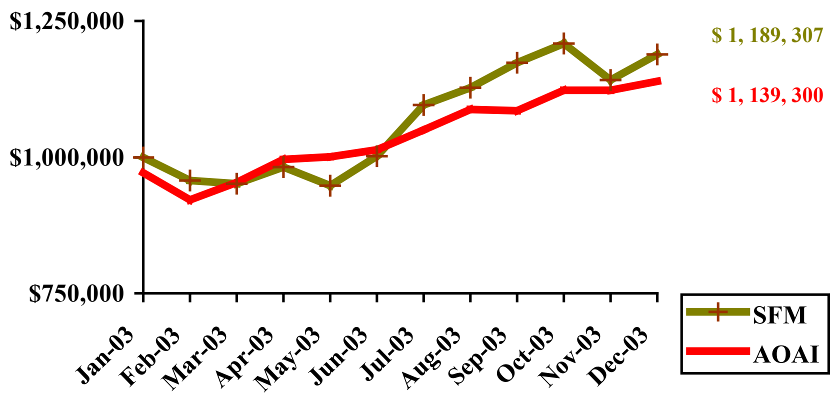
SFM_{MP} performance table since inception

Q 2003	$ Valuation	% SFM Quarterly return	SFM return since inception	All Ords Accumulation Index	% AOAI Quarterly return	AOAI return since inception
Mar Q 1	950,830	-4.92		14,888	-4.61	
Jun Q 2	1,002,330	5.42		15,818	6.25	
Sep Q 3	1,173,601	17.09		16,941	7.10	
Dec Q4	1,189,307	1.62	18.93 %	17,787	4.94	13.99 %

Selector Fund Start Date 21/01/2003

Comment: The performance of the fund on a quarterly basis is illustrated in the table above. While our annual target of compounding at 15% has been bettered in our first year, albeit with a tail wind, we have also experienced considerable volatility. We expect this volatility; as it goes hand in hand with a concentrated portfolio. The variation in returns for our first 4 quarters (in particular Q3) highlights the significant impact that a large exposure to a winning (or losing) stock selection will have on a concentrated portfolio. This is central to our investment style. We are stock selectors and as such we have confidence in taking on and holding larger positions in fewer stocks. SFM

Value of $1.0M invested with SFM_{MP} since inception



Overview: We visited 29 companies in the quarter, some for the first time and others for an update. In contrast to Q3 we made only one adjustment to the portfolio. Visiting a new company for the first time is exciting. We go armed with the knowledge we can gather from public information, and often with a few preconceived ideas. There are so many questions to ask and an hour or two only scratches the surface. But without a doubt, that time and effort is of great value every single time – whether we act or not and it's amazing how often the preconceived ideas will change. We visited a "boring" company that happens to be a monopoly. It is a simple business, its branding is "nearly a household name" and it has a strong fully franked yield. It also had a legitimate reason to come to the market. If you're into the market and discovering companies then you will understand that this type of visit is as

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rewarding as watching Steve Waugh hit an Indian paceman for six. And if you're a cricket fan of sorts you'll also know that occasionally Steve Waugh took one on the body. In our last SFM Q3 newsletter we talked about the "two steps forward and one step back" recovery of **Aristocrat Leisure (ALL)**. **ALL** managed to deliver the equivalent of a body blow in Q4 and while you'll expect it, each one still hurts. We talk about both of these experiences from Q4 2003 below. SFM

We spoke about bumps and bruises that are delivered in all walks of life from cricket to investing. **Aristocrat Leisure (ALL)** certainly hasn't missed us on this front, dropping from $2.60 to $1.60 in Q4. Law suits, rising $A, slowdown in gaming, smoking bans, and more staff upheavals make this stock volatile. Having said that, even though the recent appointment of Paul Oneile as MD, who previously worked at United International Pictures, raised more questions than provided answers it starts the process of change. The franchise remains intact (licences to sell gaming machines and product are a major barrier to entry) and we believe extreme negative sentiment is priced into **ALL**. We continue to be comfortable in holding **ALL** and aim to meet Paul Oneile in Q1 2004. SFM

Sometimes not all the ducks line up in a row for an investment to be made. In the case of **AAV Limited (AVV)*** the value was apparent but we required more confidence that we were on the right track. As such we made an initial small investment, which we subsequently topped up as both the business and management proved that the value was both real and substantial. The reason why **AVV** remained undiscovered by the market was its entry onto the exchange. **AVV** came to market via a backdoor listing through ISIS Communications – a dud that would have scared off the bravest day trader. **AVV** is the leader in VHS, CD, DVD production in Australia. Its founder and Chief Exec has been in the industry and business for 20 years and is a Director of Special Broadcasting Services (SBS - Channel 0). We found **AVV** in our travels and met management before buying. We saw it as an opportunistic situation where the market was simply miss-pricing the business and its ability to generate both strong cashflow and pay good dividends. SFM ** code is not a typo*

Floats have become "all the rage" over the past two Quarters. And while we don't close our eyes to opportunities we are wary of the promises and blue sky that promoters bring to the table. Occasionally we take notice. The float of **Boom Logistics**, **IOOF** & **SAI Global (SAI)** were worthy of consideration and one's we intend to follow. There were a host that just wouldn't get us interested. We alluded to **SAI** earlier – it has all the hallmarks of a great stock – simple, monopoly, yield and annuity income stream model. We held off until we got to meet with management. Having spent two hours with COO Tony Scotton we gained a clearer picture of a business making the transition from mutual status to a professional culture. Good organic growth sprinkled with conservative acquisitions (albeit offshore which we view as the major risk) will drive this business. Scotton described the product as "essentially boring" – we view it as an essential monopolistic service with a very low risk profile. The parent company Standards Australia owns 40% (relies on dividend income for funding) and as local institutions are moving towards a collective 20% (then higher) this will become a tightly held situation. SFM

Patrick Corp (PRK) - Chris Corrigan can't get enough of **Virgin Blue (VBA)** putting his hand up to acquire more in the float at $2.25 and providing the group with a 45% equity interest in the $2.4b discount airline. **PRK** has done very well out of the deal so far, though Sir Richard Branson has certainly done a lot better. That said, Corrigan is not one to underestimate and we rather back **PRK** and their proven management ability with **VBA** in it than investing directly in the discount airline. SFM

Petsec Energy (PSA) We see natural resources as an emerging theme in the market place. Our reading suggests to us that the USA is on the brink of a natural gas crisis which could result is prices being sustained above $10pmcf from the current levels of around $5pmcf. US discoveries are simply not replenishing supplies as quickly as the growth in demand. Most new housing construction includes natural gas central air conditioning. This impact was felt in summer. We watch with interest, as a harsh winter could be the catalyst for such a crisis. The consumer and utilities will come under pressure

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if such a scenario pans out. We simply note this as a backdrop to the drilling success unfolding for **PSA** – a beneficiary of higher prices. While **PSA** is not without risk our experience is that yesterday's heroes go overlooked for sometime. This often represents opportunity for those prepared to look forward, particularly if management have gained experience rather than baggage. We are backing Terry Fern.
PSA and Terry Fern climbed to spectacular heights in the 90's prior to a near death experience. Today, they and investors may just be better off for it. In fact, we believe the "NDE" was well handled. The Australian company was quarantined from US bankruptcy proceedings and survived with $20 M + cash and a data base worth in excess of $10M. Terry Fern has proven to be a stayer. Having paid 16c a share Terry took the ride to >$7 and back to 11c. It appears Terry has a second chance to reap the benefits of his unchanged 26% holding in **PSA**. SFM

Cochlear (COH) We took a trek across town to "hear" what was really going on at the **COH** AGM, rather than get the second hand info passed around the market and papers. **COH** is the world market leader and is perhaps Australia's most successful company in terms of pioneering a device and taking it onto the world stage. **COH** has a first class balance sheet and board and post the profit downgrade trades on short-term issues. If **COH** can grow the number of implants and EPS by 20% on average over the next 5 years then EPS will jump from $1.10 to $2.74 & with dividends likely to follow suit from 77¢ to $1.92. As Peter Lynch (Fidelity Fund, "One up on Wall Street") noted " stocks that take you the farthest in the long run tend to give you the most bumps and bruises along the way". We like the company, knowing there are issues to be resolved but this is a rare opportunity for the patient investor. SFM

Big Picture: As we mentioned very little new investment activity was undertaken in the Fund in Q4. Rather than viewing this as a lack of activity it really indicates that good investment opportunities are rare. We look for themes that unfold and tie in with stocks that have financials we like to see, including high ROE (return on capital invested referred to as equity), ROA (return on assets), and a major shareholder with a focus to grow the business - Gerry Harvey refers to this as having "blood in the business". **STW Group (SGN)** (the renamed John Singleton Company) and **Ten Network (TEN)** are examples. Our Fund holds 5.6% and 4.6% respectively in each stock. While we have no control over how the market will value them on any given day what we are interested in is the underlying growth in the business profits and the brand franchise. No surprise that Singleton is a big shareholder in **SGN** and Canwest is a dominant shareholder in **TEN**. Our preference is to buy when there is a big shareholder who thinks like we think. Great management is critical, John Singleton identified his own weaknesses and filled the void with Russell Tate, thankfully one of Singleton's great strengths is picking people – Tate is a proven performer and one of the best in the ad business. Canwest also went after the best management for **TEN –** Nick Falloon's appointment was the turning point. The corollary to this adds even greater strength to the argument. Eg. **Brazin**, we attended the AGM and left uninspired and questioned the business on many fronts – the biggest question was over management. Many people saw the demise of music stores profitability coming some time back but the real damage was done by a management team that failed to position for change. These are lessons we learn from. We look for great management teams. To have a bad manager in charge of a great business will at the very least damage or retard the brand**. NAB** may be another example, and being "big" doesn't necessarily provide safety just ask **Parmalat, Shell, Adecco** and **Hollinger** shareholders. As an aside, books worth reading are the biographies on John Singleton, Gerry Harvey, Packer, and Sir Richard Branson etc. These are not only a great read, but they also go a long way towards explaining why success is not achieved overnight (just like successful investing doesn't happen overnight) and why really successful people are worth backing. SFM

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Selector Diary Q4 2003

Companies visited in Q4 2003		
02-10-03	Cullen Resources	CUL
02-10-03	Oroton Group	ORL
07-10-03	Solution 6 Holdings	SOH
08-10-03	TEN Network	TEN
14-10-03	Record Investments	RCD
17-10-03	Marengo Mining	MGO
20-10-03	ITL	ITD
21-10-03	Cochlear	COH
23-10-03	Australian Gas Light	AGL
28-10-03	Millers Retail	MRL
29-10-03	Macquarie Infrastructure	MIG
29-10-03	Infomedia	IFM
30-10-03	Baycorp Advantage	BCA
04-11-03	KAZ Group	KAZ
05-11-03	Gowing Bros	GOW
10-11-03	MIA Group	MIA
11-11-03	DCA Group	DCA
13-11-03	Virgin Blue	VBA
14-11-03	Westfield Holdings	WSF
17-11-03	Brazin	BRZ
18-11-03	Pharmaxis	PXS
19-11-03	Patrick Corporation	PRK
24-11-03	Prime Television	PRT
25-11-03	Harvey Norman	HVN
27-11-03	Macquarie Airports	MAP
02-12-03	Medivac	To List
03-12-03	Gallery Gold	GGN
04-12-03	SAI Global	SAI
09-12-03	Ventracor	VCR
23-12-03	National Hire	NHR

SFM MP Alphabetic order of Top 10 Holdings		
1	ABC Learning	ABS
2	Aristocrat Leisure	ALL
3	ION Limited	ION
4	Kaz Group	KAZ
5	Peppercorn Inv Trust	PIV
6	Reece Australia	REH
7	Sigma	SIG
8	STW Communications	SGN
9	Suncorp	SUN
10	Ten Network	TEN

SFM MP Activities during Q4 2003	
Share transactions	0
Purchases	1
Sales	0
Takeovers	0
# Investments in fund	24
# Investments > 3% fund	15
# Anchor stocks	9
# Situations	10
# Turnarounds	5
New Public Listings	-
Placements	-
Other Issues	-
Company visits	9
Company presentations	17
New Companies Reviewed	12

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We have moved: Selector Funds Management Limited has moved to new premises in the Sydney CBD. We are now located in the historic Burns Philp Building which dates back to 1896. The building was designed and constructed for Burns Philp by architect brothers George and Arthur McCredie, who where also responsible for the tiled facade Mark Foys building and the construction of underground telephone cable tunnels in the Sydney CBD – still in use today. In 1894, George stood for election in the NSW Legislative Assembly and won the seat of Central Cumberland as an independent free trader and an advocate of female suffrage. He lost his seat the following year and returned to work, but in 1900, the State Government called upon him to help clean up the City of Sydney when there was an outbreak of the Bubonic Plague. In gratitude for his work, the people of Sydney presented George with a shield that is now held in the Powerhouse Museum. Our building is considered to be one of a kind in Sydney reflecting Romanesque qualities of the early American colonial architecture, although the Australian Heritage Committee considers it to be Gothic. Please feel free to drop in for a cup of tea. **Level 3 Burns Philp Building 7 Bridge Street, Sydney NSW 2000**. SFM

Corey Vincent outside Selector Funds Management Limited new Sydney head quarters

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>
> Peter Lynch

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