



Challenger Funds Management

(a subsidiary of Challenger Financial Services Group)

- Manages **Australian property securities** for MLC, since 2004
- Manages \$19 billion, across the company, as at 31 December 2009
- Part of the Challenger Financial Services Group which has origins dating back to 1984.

Originally part of HSBC, the Property investment team moved across to Challenger as part of the 2005 acquisition. Since then the team has continued to grow and today the Challenger Real Estate Securities team is one of the most experienced and well resourced in the country.

The 2006 strategic alliance with multi-national real estate investment firm, Heitman further strengthened Challenger's property capability through the provision of specialist localised knowledge of European and American property markets.

Why has MLC chosen Challenger?

MLC uses Challenger because it has a well-credentialed team that applies a clearly enunciated "business cycle approach" which is coupled with detailed bottom-up property trust research. Challenger manages a high conviction portfolio of 15 stocks on behalf of MLC.

Philosophy on investing

Challenger believes that mis-pricing opportunities arise in the listed property market at the macroeconomic, industry and individual trust levels. Challenger's Real Estate Securities team undertakes comprehensive research of both top-down and property trust specific fundamentals in order to identify these mis-pricings.

Challenger's investment approach identifies the major trends in the economy, and looks at how these trends will influence financial and property markets. By analysing both global and domestic economic prospects, they aim to position investment portfolios to take advantage of future economic developments. The level of exposure to a sector (for example retail or office) is based on their 'top-down' business cycle and property market analysis, combined with 'bottom-up' company analysis. Their 'bottom-up' fundamental analysis allows them to identify those stocks they expect will deliver superior performance over the medium to long term.



John Longo
Co-Head Real Estate Securities



John White
Co-Head Real Estate Securities

Investment process

The top-down analysis of the external business cycle and property sector fundamentals is the primary driver of the property sector exposures in the portfolio. The Challenger team developed a property business cycle index to guide property sub-sector weightings in the portfolio and the direction of the fundamental sector and individual security research they conduct. The index models a range of economic factors (e.g. interest rates, economic growth, retail sales, business and consumer surveys) to produce a ranking of the main property sectors: office, retail, industrial and residential. Each property sub-sector is analysed in depth, including an examination of the demand and supply forces in the respective markets and their likely impact on future occupancy, rents and capital gains.

The investment team also reviews relevant external research on the property market and

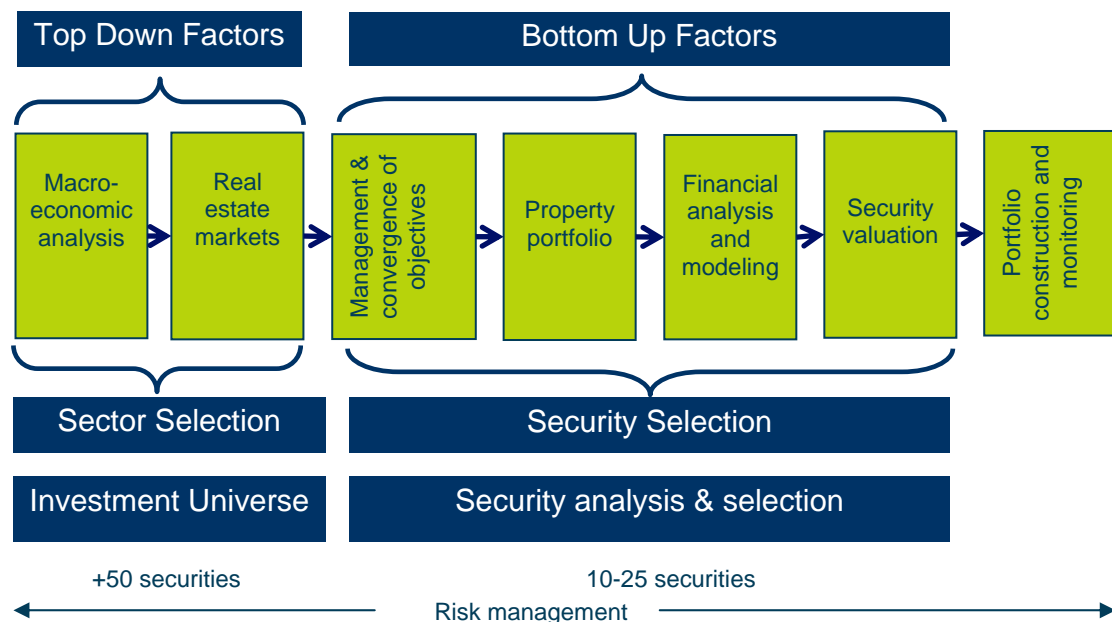


sector trends, including the direct property intelligence from Challenger’s direct property team, to identify consensus views on markets and potential mis-pricing opportunities.

Challenger’s research of individual trusts covers a range of qualitative and quantitative factors. Key qualitative factors are management and the convergence of objectives between management and unit holders, which the team assesses via frequent interviews with trust management. Aside from establishing the existence of quality management, Challenger seeks to confirm that management has a clearly defined trust strategy; a high level of focus and knowledge; a proven track record, and; a robust organisational structure.

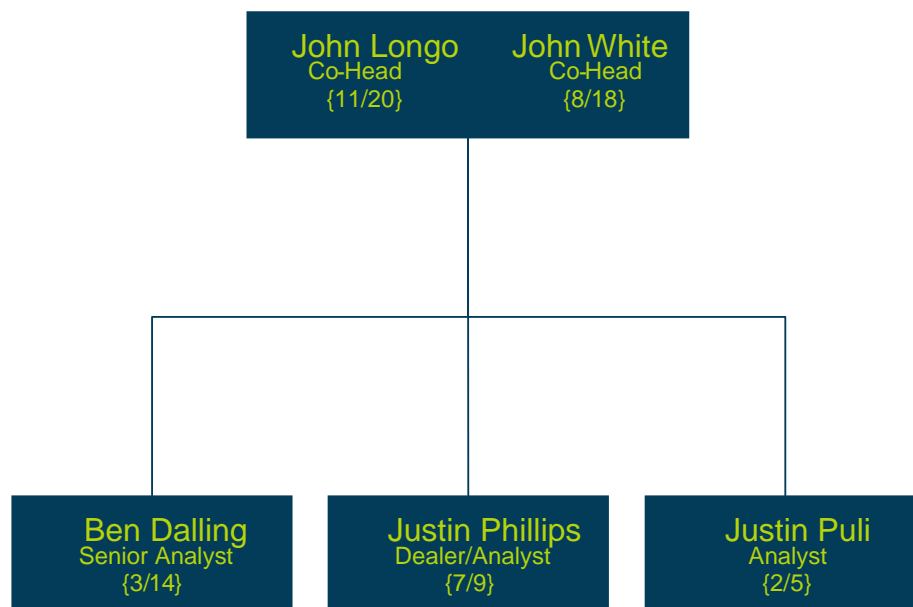
Challenger’s quantitative research of individual trusts involves proprietary financial and valuation modelling. Financial modelling includes historical analysis and property income forecasts. Challenger’s valuation methodology relies on two models –a net present value model for the capital markets’ pricing of securities and a net asset value approach which prices the intrinsic “bricks and mortar” value.

Challenger’s listed property securities investment process is summarised in the following diagram.



Investment people

The portfolio is managed equally by John Longo and John White who are both Co-Head of Real Estate Securities. The team moved from HSBC to Challenger in 2005 with the acquisition of HSBC’s investment management team.



{Years with Challenger/HSBC Industry experience}



John Longo – B. Bus. (Prop), AAPI, ASIA

As Co-Head Real Estate Securities, John is responsible for the composition and stock selection of the portfolio. John has 20 years of industry experience. He held the position of Senior Investment Manager – Property, HSBC Asset Management for 7 years prior to their acquisition by Challenger in 2005. John graduated from RMIT (Victoria University) with a B.Bus (Property) in 1999.

John White – B.Bus (Land Econ.), Grad. Dip. Applied Finance, AAPI, FFin

As the other Co-Head Real Estate Securities, John is also responsible for the composition and stock selection of the portfolio. John has 17 years industry experience. He held the position of Senior Investment Manager – Property, HSBC Asset Management for 4 years prior to their acquisition by Challenger in 2005. John graduated from with a B.Bus (Land Economics) from the University of Western Sydney in 1991.

Ben Dalling – B.Eco (Hons), M. Com (Finance).

Ben is an analyst for Real Estate Securities. Ben joined Challenger in 2006 as a Senior Analyst from Goldman Sachs JBWere where he was employed as a Real Estate Equity Analyst. Prior to joining Goldman Sachs JBWere, Ben worked for HSBC Securities where he was a listed property trust analyst. Ben holds a Master of Commerce from the University of Melbourne (completed in 1994) along with a Bachelor of Economics (Hons) which was completed at La Trobe University, Melbourne in 1996.

Justin Phillips – Grad. Dip. App. Fin (SIA).

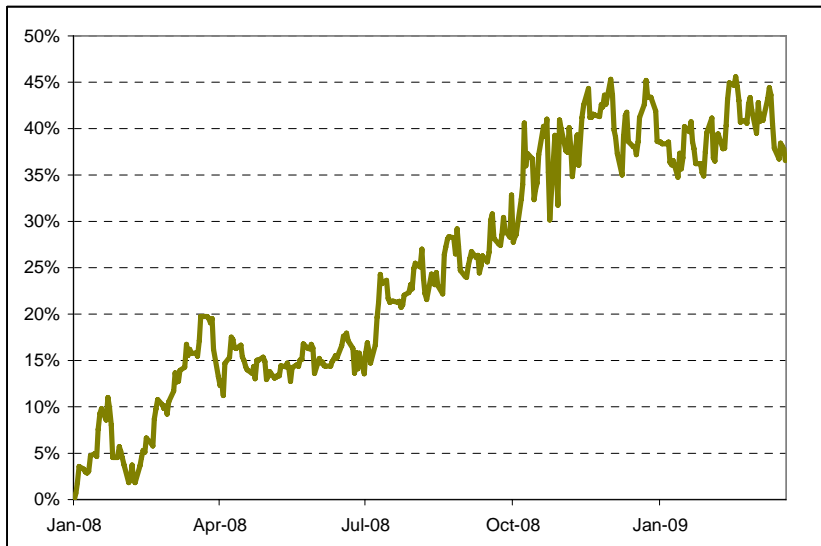
Justin is dealer and analyst for Real Estate Securities. Justin joined Challenger as part of Challenger’s acquisition of HSBC Asset Management in May 2005. Prior to joining HSBC in 2002, Justin was a futures dealer with Macquarie Bank, specialising in broking Share Price Index Options and other equity derivative products. Justin holds a Graduate Diploma in Applied Finance and Investment from the Securities Institute of Australia (completed in 1999). Justin is a Level III candidate in the CFA program.

Justin Puli – CFA, B. Com (Hons).

Justin is an analyst for Real Estate Securities. Justin joined Challenger in October 2006 and is responsible for stock research and database management. Prior to joining Challenger, Justin was employed at Glebe Asset Management where he was responsible for equity and credit research of listed companies. Justin began his career at HSBC Asset Management and also gained property experience at ANZ Banking Group. Justin completed his Bachelor of Commerce (Honours) (Accounting and Finance) at Monash University in 2003 and is a CFA Charterholder.

Stock story - CFS Retail Property Trust (CFX)

CFX Relative Performance since 2008



Source: IRESS, Challenger Real Estate Securities



CFS Retail Property Trust (CFX, formerly CFS Gandel Retail Trust) a retail sector specific Australian Real Estate Investment Trust (A-REIT) which invests in high quality regional and sub-regional shopping centres across Australia. It boasts some of Australia's premier centres including Chadstone in Melbourne, Chatswood Chase in Sydney and the Myer Centre in Brisbane. It is managed by subsidiaries of the Commonwealth Bank

Challenger purchased the stock and moved to an overweight position in mid to late January 2008, remaining overweight over the year and continuing into 2009. The following points explain why they hold the stock from both bottom-up and top down points of view.

Top down - Economic and Property sector

- The security is solely invested in the Australian retail property market. The macroeconomic outlook for Australia is more positive than other regions and the consumer sector has proven to be and is expected to remain resilient.
- Retail property markets, particularly in the regional mall space is characterised by high occupancy, strong relative demand and consistent rental growth.
- Supply of new competition is limited, particularly in this capital constrained environment.

Bottom up factors

- CFX has the highest quality shopping centre portfolio in the A-REIT space. Whilst Westfield (WDC) has strong shopping centres, it has significant exposure to the difficult markets of the US and UK.
- Management is undertaken by Colonial (a wholly owned subsidiary of the Commonwealth Bank).
- The financial characteristics of the stock are strong and stable. It has low gearing, a stable dividend and in-built rental growth prospects from existing tenants and potential capital expenditure.
- The relative expected return is attractive from a risk adjusted basis, trading at a discount to intrinsic valuation.

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