

Wallara is an Aboriginal word meaning “clear headed” and reflects the firm’s disciplined and distinctive approach to investing.

Wallara Asset Management Pty Ltd

- Manages **Australian shares** for MLC, since 2004.
- Manages \$3 billion, across the company, as at 30 September 2008.
- Origins dating back to 1995.
- Based in Melbourne, Australia.
- Entirely owned by investment team.

Why has MLC chosen Wallara?

MLC use Wallara because they have a clearly articulated philosophical belief that is based on shareholder value analysis. The experienced investment team combine to create an intellectual resource committed to investing in a fashion complementary to MLC’s strategy. Wallara manage a high conviction, large-cap, growth oriented portfolio of 25-30 companies with a low level of turnover.



Peter Wetherall
Managing Director

Philosophy on investing

Wallara is a bottom-up, active manager of Australian equities. Through their application of shareholder value analysis techniques they aim to identify stocks expected to deliver above average growth in shareholder value that they can purchase at a reasonable price.

They believe that superior returns are achieved by investing in companies with a strong financial position, an ability to reinvest capital at rates above the cost of that capital and past records of achievement. These preferences result in a portfolio with growth characteristics. Wallara is not a trading oriented investor and portfolios have only moderate turnover.

Investment process

Wallara’s stock research is aimed at attaining insight into the factors that drive shareholder value creation. This requires analysis of both qualitative and quantitative considerations. Qualitative analysis involves understanding the key drivers of a company’s financial performance; the quality of management; the outlook and structure of the industry it operates in; asset quality; the sustainability of any competitive advantage it might have; and, the presence of expansion opportunities via the investment of capital in new assets that will deliver returns above the cost of capital.

The quantitative analysis Wallara conducts involves the collection and analysis of at least eight years of historical company financial data to understand the historical performance of the company and the key financial performance drivers. Wallara then prepares two years of projected income, balance sheet and funds flow statements using in-house developed forecasting spreadsheets. The objective of this detailed analysis is to gain a deeper understanding of a company’s activities and to isolate key areas for discussions with

company management. It also ensures they have internally consistent financial statements, which is important given their focus on returns as the principal measure of financial performance.

Having created the required forecast financial statements, Wallara then imports the financial data into an internally developed based shareholder value analysis model. This software is used to calculate the cashflow return on investment (CFROI), cost of capital and DCF-based valuation of each company in their universe (around 120 of the largest listed companies by market capitalisation). The shareholder value analysis approach is quite sophisticated and explicitly takes into account the returns a company is generating, its sustainable or natural level of growth, its sustainable competitive advantage, its financial structure, the age of its depreciating assets and its size. Cash measures, not accounting based measures, and adjustments, are used to remove the impact of distortions such as off balance sheet financing, the impact of inflation, the life of depreciating assets, the effect of non-cash gains or charges and so on. One of the main advantages of the CFROI measure is that it levels the performance measurement playing field and allows meaningful assessment of performance over time and across different industries.

Once this research is completed, stocks in their research database are ranked according to a range of criteria and those considered for inclusion rank strongly against four key purchase criteria. These are:

- Qualitative assessment of outlook for shareholder value creation (i.e. management's track record of wealth creation future strategy). Wallara favour companies with a consistent record of valuation creation.
- Trend in Cashflow Return on Investment (CFROI). Wallara favour a rising trend.
- Trend in Consensus Earnings Revisions. Wallara favour a stable or rising trend in consensus forecasts.
- Price relative to Valuation. While Wallara favour companies that are cheaply priced, the stronger the potential for value creation the less discount to valuation they need.

Accordingly, stocks favoured by Wallara for their potential to generate very good investment returns are those which have:

- strong signals of future value creation indicated by a rising trend in CFROI;
- rising consensus earnings revisions;
- abundant opportunities for investing capital in projects that will deliver returns above the cost of capital; and,
- skilled management able to take advantage of these opportunities.

The portfolio is concentrated to ensure only the best ideas are put to work, but without losing the risk reduction benefits of portfolio diversification. The number of holdings is between 25 and 30 and guidelines are applied to control risk by limiting the maximum and minimum exposure of the portfolio to individual stocks and selected sectors.

Investment people

Wallara was founded in 1995 by Peter Wetherall, and consists of the following investment professionals.

Staff	Position	Qualifications	Started with Wallara	Industry Experience
Peter Wetherall	Managing Director	B.Eng. (Mining) Hons B.A. (Phil, Politics & Economics)	1995	27
David Rosenbloom	Director	MBA BBA (Accounting)	1999	11
Greg Marks	Senior Investment Manager	B.Bus Studies (Accounting) M.Ap.Fin	2000	13
Ivan Reyneke	Senior Investment Manager	MBA B.Sc (Statistics & Actuarial Science) Chartered Financial Analyst	2004	12
Steven Lambeth	Investment Analyst	B.Com (Finance) Hons Chartered Financial Analyst	2004	8

Stock story

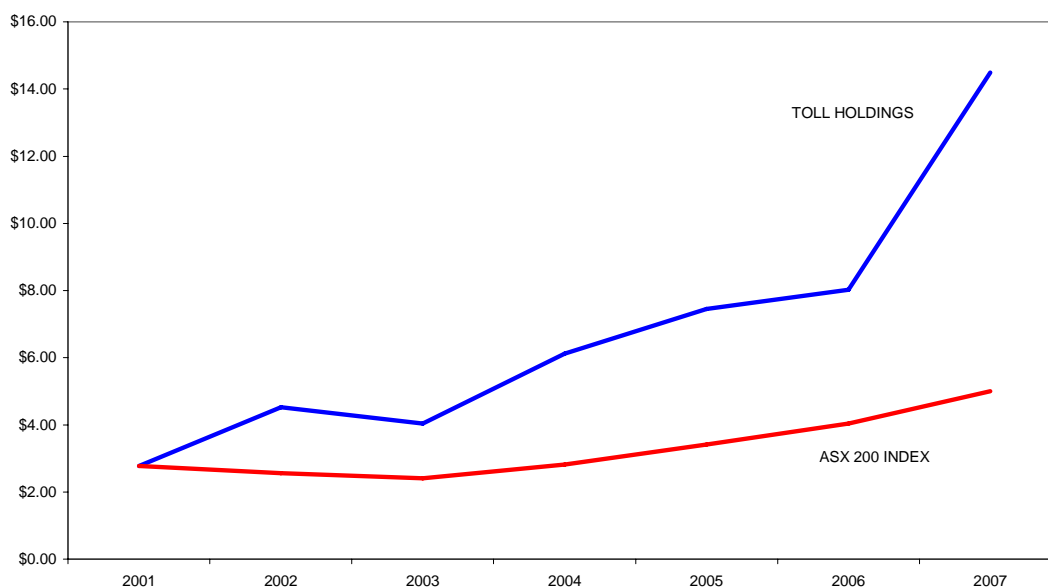
Toll Holdings

At the height of the tech boom in 2001 who would have thought a trucking company would have been a stand-out investment opportunity? This is when Wallara first purchased shares in Toll Holdings, and as the chart shows, since then this share has generated a compound return of 32%pa compared with 10%pa for the broader market. Wallara's analysts at that time were searching for companies that had the potential to be major beneficiaries of the IT revolution. They became interested in the transport and logistics industry as an area where new technology could dramatically change the competitive landscape, and Toll in particular given its commitment to investing in technology and innovation. As the expectations of large logistics customers became more sophisticated, smaller privately owned transporters would struggle to compete.

Toll's financial performance up to that time was impressive. A combination of organic growth and acquisitions had seen sales expand from \$119m in 1994 to \$1,360m in 2000, while cashflow returns on investment (CFROI) had remained steady at around 15%, well above the company's cost of capital. Historically, Toll management had created shareholder value at the rate of 19% pa, which is well above average. Projections of future financial performance were positive, the discounted cashflow valuation of the company was higher than the share price, and it met all Wallara's key purchase criteria.

Since then Toll has expanded to include rail and port assets and operations in New Zealand and Asia. The rail and port facilities have recently been spun off to shareholders in a new structure named Asciano, leaving Toll with an ungeared balance sheet with which to fund further growth. The prospects for both Asciano and Toll remain positive in Wallara's opinion.

TOLL HOLDINGS vs ASX200 INDEX



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