BAIOCCHI GRIFFIN
PRIVATE WEALTH

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Welcome to the first issue of the *Baiocchi Griffin Private Wealth* Investment Update

We're pleased to welcome you to the first issue of our quarterly Investment Update. The purpose of this publication is for us to share with you our views on the current state of economic and financial markets, and to communicate any other relevant information. Your feedback is important to us, so please feel free to contact us with comments or suggestions. We trust you will find this newsletter interesting and informative. Kind regards, Justin & Ray.

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Looking ahead to 2013, what the year might hold for markets and the economy

"…too late to save the promised federal government surplus."

In terms of the impact on financial markets, 2012 was an eventful year.

The year was most certainly dominated by the ongoing crisis in parts of Europe, with particular emphasis on southern European nations such as Italy, Spain and Greece. Though immediate concerns over the survival of the Euro were eased by the actions of the European central bank, it certainly isn't the end of Europe's fiscal woes.

At the same time as Europe struggled with its debt levels, Chinese economic growth slowed considerably. This economic slowdown was largely deliberately engineered by the Chinese authorities, who had to act to cool the rising property market, and they appear to have been successful in slowing the economy to an appropriate speed.

This slowdown, as well managed as it was, hurt Australian mining companies, who saw prices for their products collapse through the year. Fortunately as Chinese growth has picked up, so have commodity prices, although too late to save the promised federal government surplus.

Baiocchi Griffin Private Wealth

Looking ahead to 2013

Despite the issues in Europe and elsewhere, many of which are still not resolved, the Australian stock market recorded strong gains over 2012, with the majority of these occurring in the second half of the year. Although the growth was concentrated in a handful of stocks, including the banks, healthcare sector and a number of large industrials, the index managed to grow by just over 14% for the year. This credible performance saw the index end the year at 4,648 points, but still a long way short of the 2007 market high of 6,792 in October 2007.

The global economic situation has improved, although the Australian economy still faces a number of challenges

The outlook for 2013

Looking ahead to 2013, our view could be generally described as 'conservatively optimistic'. That is, we recognise sufficient signs of recovery in the United States which gives us hope that the US, still the world's largest economy, might finally have turned the corner. With an improving housing market, and gradual falls in unemployment, the signs of stability in the US are evident. The major risk however is the political process in the US, with Republicans and Democrats exhibiting a deep (and worsening) divide on many issues, but particularly on the fiscal approach adopted by the US. This political risk may undo the positive effects of an improving housing market and more confident consumer.

The 'fiscal cliff'

To a degree the US has managed to avoid the 'fiscal cliff' which looked set to derail the economic recovery at the start of 2013, however lawmakers in the US must still deal with the debt ceiling issue in early March. We again expect a last-minute compromise which unnerves both markets and investors.

With regards to the Australian domestic economy, we expect the coming year to be reasonably tough for both businesses and households. The high Australian dollar and slowdown in the resources sector leaves the economy in a fairly weak state, and we expect economic growth for the year to reflect this. The Reserve Bank of Australia (RBA) is attuned to these concerns, as evidenced by the cuts in official interest rates in the second half of last year.

While the interest rate cuts will assist in lowering the cost of credit for business and households, it may not necessarily lead to an increase in demand for credit, which would usually be the outcome. This is due to the fact that the past few decades of over-borrowing has left little scope for increased borrowing by business or consumers. In fact, there has been a shift in emphasis among Australians to lower their overall debt levels, actions which work against attempts by the RBA to stimulate economic growth.

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Impact on the markets

Given the headwinds facing the Australian economy and the continuing issues overseas, you might be led to believe that this bodes poorly for investment returns for 2013. Surprisingly there is actually a relatively low correlation between economic growth and stock market performance. An economy can be growing slowly, yet still register acceptable returns on listed investments.

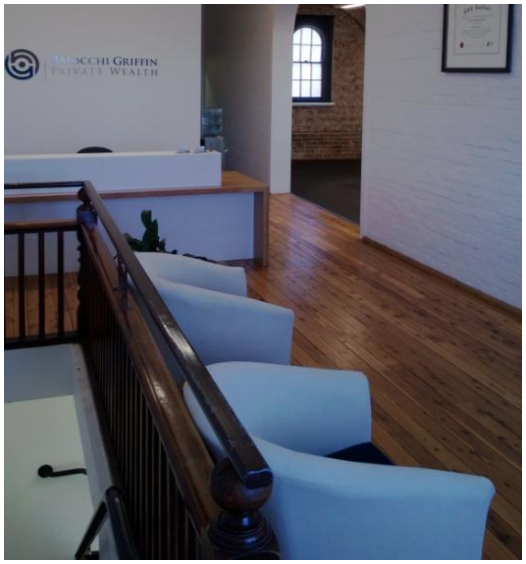
The performance of the US and Chinese stock markets during 2012 illustrates this point. Despite the fact that the US economy grew by only 2% for the year ended 30 September 2012, its stock market increased by 13.3% over the same period. The Chinese economy on the other hand, grew by 7.4% over the same period, yet its stock market fell by nearly 17%.

On the downside, the interest rate cuts late last year will have an impact on the amount of income earned by fixed-interest investments. Offsetting this however should be appreciation in the value of shares, which usually benefit in a falling interest rate environment.

Central Bank action

A longer-term issue is how central banks in the US, Europe, the UK and Japan manage their expanding balance sheets. Since the onset of the global financial crisis in 2008, these central banks have attempted to stimulate economic growth through quantitative easing (often called 'money printing'). The banks use this newly-printed money to buy government bonds, thereby keeping the interest rate on government debt low, but at the same time building up extensive holdings of government debt. For example, the US Federal Reserve now owns $1.7 trillion of US government bonds. While this strategy has been largely successful in terms of keeping interest rates low and stimulating economic growth, at some point action will need to be taken to reverse the monetary easing and shrink central bank balance sheets. If not done carefully, this will increase interest rates and push those economies back into recession. We will be closely watching this issue in coming years.

Decisions taken by central banks have played a crucial role in stabilising the global economy



We thank you for your support and look forward to working closely with you in the years to come.

Business Update

We would like to take this opportunity to thank you for your continued support over the past few months. We would particularly like to thank you for your co-operation in returning all the necessary documentation required to cease the relationship with Capricorn Investment Partners. We are in the process of transferring all investment accounts, transactions and records onto the new systems, a process which will be complete by the end of March.

We are excited about the changes in our business, and the continuing opportunity to be of service to you. We wish you all the best for 2013.

Facts & Figures at a Glance

	This quarter	Last quarter
Australian inflation rate	0.2% ⇧	1.4% ⇧
Australian unemployment rate	-0.1% ⇩	0.2% ⇧
RBA Cash rate	3.00%	3.50%
ASX 200 Index	5.95% ⇧	7.12% ⇧
MSCI World Index (ex-Australia)	2.06% ⇧	6.13% ⇧
Australian $ vs. US $	$1.0384	$1.0464
Australian $ vs. UK £	$0.6428	$0.6437
Australian $ vs. Euro €	$0.7868	$0.8093