



## DDH Fixed Interest Fund

### Performance Report for the Quarter Ended 31 December 2009

#### Investment objective

The DDH Fixed Interest Fund invests in the QIC Australian Fixed Interest Fund which aims to exceed the performance of a portfolio of highly rated Australian fixed interest securities by investing in a diversified, medium risk portfolio of Australian and international higher yielding fixed interest securities and derivatives.

#### Commentary and outlook

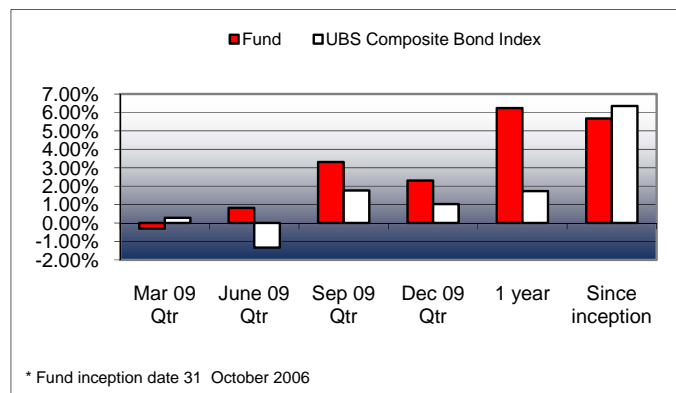
The performance of the DDH Fixed Interest Fund is set out below. Refer to the attached performance report from QIC. Please note that the performance figures quoted in QIC reports relate to the underlying QIC wholesale funds.

#### Performance

	3 months %	6 months %	1 year %	2 year % p.a.	3 year % p.a.	Since Inception % p.a.	QIC Fund Since Inception % p.a.
Total return	2.31	5.69	6.24	7.43	5.85	5.67	7.75
Growth return	1.07	3.09	-2.72	1.33	-0.30	-0.60	
Distribution return	1.24	2.60	8.96	6.10	6.15	6.27	
Benchmark	1.04	2.82	1.73	8.14	6.56	6.35	7.55

#### Performance notes:

1. DDH Fixed Interest Fund inception date - 31 October 2006.
2. QIC Australian Fixed Interest Fund inception date - June 1994.
3. DDH fund returns are calculated after fees have been deducted and assuming reinvestment of distributions. No allowance is made for tax.
4. QIC fund returns are before investment management fees.
5. Fund benchmark - UBS Composite Bond Index



#### Unit Price as at 31 December 2009

Entry price (ex distribution)	\$0.9819
Exit price (ex distribution)	\$0.9811

#### Income distribution

The distribution for the quarter ended 31 December 2009 is 1.20 cents per unit. Details of the final tax components of the distribution will be advised to unitholders after 30 June 2009.

#### Asset allocation

	As at 31-12-09 (%)
Australian fixed interest	100

## QIC Australian Fixed Interest Fund

### Fund details at 31 December 2009

#### Profile

Description	The Fund is a domestic fixed interest portfolio that is actively managed by the QIC Global Fixed Interest team to lift returns and minimise risk.
Objective	To outperform the UBS Composite Bond Index by 0.80% per annum.
Inception	June 1994
Size	AUD \$303.2 million

#### Performance

Gross period returns (%)

Period	Fund	Benchmark
1 month	0.07	-0.38
3 months	2.65	1.04
Financial year to date	6.39	2.82
1 year	7.24	1.73
3 years	6.86	6.55
5 years	6.29	5.71
7 years	6.01	5.50
Since inception	7.75	7.55

#### Market Overview

##### Economic Overview

Over the quarter, credit spreads continued to narrow, driven by abundant global liquidity and market confidence that the economic recovery is gaining traction.

While headwinds are likely to remain for some time, evidence continues to build that the United States (US) economy is gradually returning to a sustainable recovery path, albeit a modest and bumpy one. The US economy officially emerged from recession in the third quarter, recording growth of 2.2% quarter-on-quarter (qoq) annualised and is on track to record even stronger growth in the fourth quarter. Housing demand has been rising faster than expected, working to quickly reduce the large inventory overhang that had built up during the crisis. This is working to put a floor under prices, which is further encouraging pent-up demand to return. Consumer spending has surprised on the upside in the fourth quarter. Other discretionary spending continues to show evidence of improved momentum, although the 'cash for clunkers' motor vehicle incentives ended in

August 2009. While the unemployment rate continues to trend higher, there is a clear slowing in the pace of job losses, with the November jobs report showing a better than expected decline in non-farm payrolls of only an 11,000.

Annual global inflation rates are rising again, mostly reflecting the movement off a low base. In the US, headline inflation is now +1.8% year-on-year (yoy), after reaching a low of -2.1% yoy in July (figures are non seasonally adjusted). Core inflation rates continue to move gradually lower, consistent with the downturn in the labour market and pullback in wages growth.

While the three Australian cash rate increases during the quarter were largely expected, Reserve Bank of Australia (RBA) commentary became gradually less hawkish and more non-committal. In particular, commentary by the RBA that the rate increases to date had been "material" caused the market to reduce the amount of tightening priced for the first half of 2010. Moreover, the decision by some major banks to pass on more than the 0.25% of the December rate increase to variable mortgage rates caused the market to rally slightly further.

A further catalyst for the rally in the front-end and steepening of Australia's yield curve came from a speech given by RBA Deputy Governor Rick Battellino in mid-December, who explicitly stated that the cash rate moves to date had moved from an emergency setting to somewhere within a "normal" range. In addition, given the widening of mortgage spreads, he explicitly stated that the current 3.75% cash rate was consistent with a pre-crisis rate of 4.75%.

##### Global and Domestic Rates Overview

Global bond yields were very volatile during the December quarter. After rallying aggressively through much of November, global bonds sold off sharply during the final two weeks of the year. US two year bond yields rose 0.19% over the December quarter, to reach 1.14% by 31 December. This was almost 0.50% higher than the all-time low yield of 0.67% reached at the end of November. The sell-off in bonds was exaggerated by declining volumes into year-end. Consistently improving economic data, in particular the much better than expected November payrolls report, suggested that yields had become considerably misaligned with fundamentals at their earlier levels. Most other major markets sold off

during the quarter as well, although US short end rates rose more than in other regions during the latest sell-off.

Long-end rates also rose aggressively during the quarter. US ten year yields rose 0.53% during the quarter, to end the year at 3.84%. United Kingdom (UK) Gilt yields rose as sharply, reaching a 2009 high of 4.08% in late December. Long end rates have lifted alongside expectations of heavy supply in 2010, while expectations that policy makers will keep policy very easy has also led to some movement higher in longer dated bonds on the basis of rising inflation expectations.

Australian two year bond yields rose 0.15% over the December quarter, but recorded significant volatility. Yields rose sharply during October, reaching a 2009 high of 4.95% late in the month, only to reverse most of those moves during the remainder of the quarter, falling to 4.41% by the end of December.

#### Global and Domestic Credit Overview

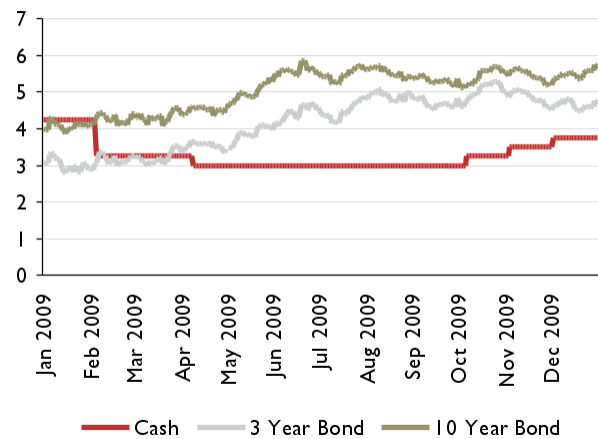
Investment grade credit spreads tightened substantially in December amid thin liquidity and positive economic data. Equity markets consolidated at slightly higher levels and concerns around the ability of businesses to refinance existing debt have declined as investment grade, and perhaps more importantly high yield names have been able to issue debt. With debt capital markets now open and businesses able to refinance the default outlook has improved considerably further supporting the strong rally in credit markets.

In the final two weeks of the month, we witnessed a few dominant themes within the credit market, albeit amid thin liquidity. Firstly, High Yield and Investment Grade corporate credit both tightened significantly, with the beta compression being the over-riding theme. This was led by a strong rally in cash bonds as investors scrambled to put new money to work before the Christmas period. Bond supply was significant in the month, however demand for these new issues far outweighed this supply with almost every deal being aggressively oversubscribed. Interestingly although most global credit markets rallied hard into year end, Sovereign credit default swap (CDS) markets continued their drift wider. This was predominately led by Greece which widened to 2.30% in five year CDS, but also Spain, Portugal and Japan amongst others came under pressure. Investors are becoming increasingly concerned about fiscal deficits and rising Debt to GDP ratios.

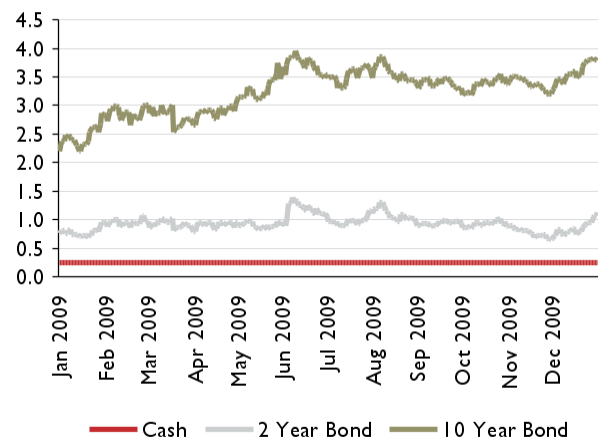
Retail investor inflows to high yield bond funds were robust, driving demand and tightening credit spreads despite strong high yield issuance of US\$188 billion in

2009. The second week of December was the seventh most active week on record for high yield primary deals and surprisingly deals continued to be priced throughout the month generally the high yield new issuance market closes down between Thanksgiving and New Year. Refinancing transactions dominated 2009, accounting for 76% of supply.

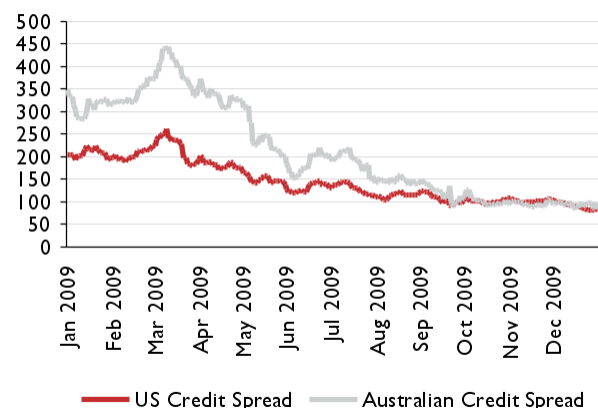
Australian Cash, 3 Year and 10 Year Bond Yields (%)



US Cash, 2 Year and 10 Year Bond Yields (%)



Investment Grade Credit Spreads (Derivative Indices) (basis points)



## Performance Drivers

During the quarter, the UBS Composite Bond Index benchmark returned 1.04% while the Fund returned 2.65%, outperforming by 1.61%. The Fund's overweight credit strategies, particularly major domestic banks and defensive infrastructure loans were the key drivers to outperformance.

Contributors to active performance (versus the benchmark) for the Fund are shown below:

### Interest Rates

#### Positive Contribution

- Australian versus UK country spread in expectation that the differential between Australian and UK bond yields will decrease.
- Australian versus US country spread in expectation that the differential between Australian and US bond yields will decrease.
- Long Australian Inflation

#### Negative Contribution

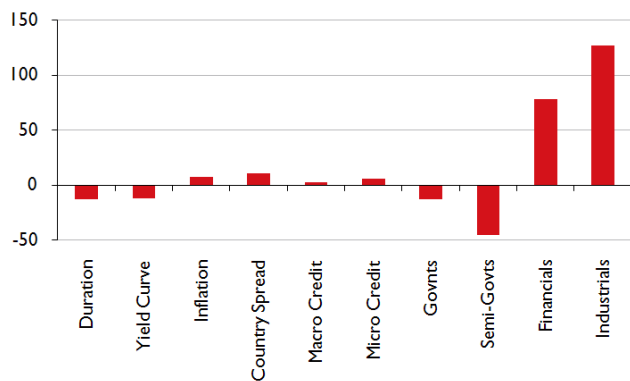
- Long Australian and short UK duration positions
- New Zealand and US yield curve flatteners

### Macro and Micro Credit

#### Positive Contribution

- Overweight selected US and Australian financials and high yield infrastructure loans
- Long selected financial names versus short selected industrial names
- Outright long and long/short single name derivative positions

#### Active performance attribution by strategy for the quarter (basis points)



## Outlook

The trajectory of the global recovery is likely to remain modest by historical standards, and the medium term outlook will be hampered by various headwinds. However, while another 'event' in financial markets can't be ruled out, there are growing reasons to believe that a double-dip in the real economy is unlikely without aggressive policy withdrawal, which seems unlikely. Indeed, the Global Fixed Interest (GFI) team believes the recovery in most developed economies during 2010, particularly in the US, will be much stronger than expected by consensus.

It is clear that global growth recovered impressively during the second half of 2009, boosted in part by a large swing in the global inventory cycle and significant fiscal measures designed to boost household spending. By their nature, the contributions to growth from these components will prove fleeting, and growth is likely to step back in the first half 2010. But there are signs of improvement in underlying final demand beginning to emerge that mean that the major economies can continue on a modest recovery path. Firstly, the amount of monetary and fiscal stimulus currently existing is unprecedented in modern times. The impact of such stimulus should not be underestimated. Secondly, while deleveraging in the banking system is likely to continue, restricting the access of credit to the broader economy, many of the earlier excesses in household balance sheets and within the US housing market are well through their adjustments.

In the US, household savings rates have risen, while improving consumer confidence is pointing to further recovery in consumer spending in coming quarters. Household incomes will remain weak, but the labour market should begin to record positive jobs growth again in early 2010, allowing a recovery in household spending. US house prices appear to have stabilised in recent months, after falling sharply over the past two years. Corporate activity appears to be improving also. Corporate profits have recovered very strongly, boosted by aggressive cost-cutting and strong productivity. Business investment appears to be rising modestly following the sharpest downturn in 50 years. With capacity utilisation around historically low levels, there is little need to aggressively expand. But with existing capital stock having been depleted through the downturn, growth can occur in coming quarters from replacement capital expenditure.

The benign global recovery should ensure enough slack remains within economies to keep inflationary pressures

away. This outlook means there will be little need for central banks to tighten aggressively during 2010. Nevertheless, GFI's view that the economic recovery will be stronger than expected means that the market could be surprised by a change in central bank rhetoric in coming months. GFI believes that these moves will be most pronounced in the US and UK.

The economic downturn in Australia has been much less severe than expected. The aggressive monetary and fiscal stimulus provided here and abroad has clearly had the desired effect of boosting spending and confidence among Australian businesses and consumers. Moreover, strong demand from China has kept export volumes robust at a time when demand from the rest of the world collapsed. Australia is experiencing a significant terms of trade shock due to sharp falls in commodity prices, and this will weigh on the economy through weaker profits and incomes. However, the stronger than expected recent dataflow in Australia, particularly the improved outlook for private business investment in 2010-11, has resulted in an upgrade to GFI's gross domestic product (GDP) and consumer price index (CPI) forecasts for Australia.

GFI has been positioned for a reassessment of how quickly the RBA will be able to move rates to neutral and beyond during 2010. Following the aggressive rally in Australian bond markets during late 2009, market rate expectations are now broadly consistent with GFI's own forecasts. GFI expects the cash rate to grind gradually higher through 2010, reaching 4.5% by the end of 2010.

The outlook for investment grade credit remains positive with the fundamental outlook continuing to improve. Stronger cash flows supported by cost cutting and an improving global economy will help drive investment grade credit spreads tighter in the coming year. The banking sector is well placed to perform strongly with continued support from regulators and improving balance sheets as poor performing loans are helped by stronger economic activity and the ability to refinance.

Demand for investment grade credit is likely to slow as interest rates are lifted by central banks, but this is likely to be in the second half of 2010. Moreover, net supply of investment grade is anticipated to be limited. In the short to medium term, we believe investment grade credit is well supported by demand and technical factors.

## Portfolio Positioning

### Interest rate strategies

Country Spread	Long Australia versus short UK at both the short and long end of the yield curve; Long Australia versus short US at short end of yield curve
Duration	Short Japan, UK and US at various tenors along the yield curve
Yield Curve	EUR, NZ and US curve flatteners, UK curve steepener

### Credit strategies

Credit Strategies	The Fund is overweight financials, particularly in the short end of the credit curve.
High Yield	We have exposure via a unit holding in QIC Global Credit Opportunities Fund.
Issuer and Security Selection	In terms of the largest active individual issuer positions, the Fund is overweight Westpac, Morgan Stanley, Woolworths and ANZ Bank
Micro Credit	The Fund has a number of long/short relative value derivative strategies across single names and bespoke portfolios,
Structured Credit	The Fund holds a small number of investment grade positions with exposure predominately to loans in the US and Europe.

### Asset composition (%)

Asset	Fund	Benchmark
Financials	58.55	26.60
Semi-Govt.	21.41	45.22
Industrials	13.92	1.75
Cash	6.12	0.00
Comm. Govt.	0.00	26.43

### Maturity composition (%)

Maturity	Fund	Benchmark
0-1 Year	18.98	12.24
1-3 Years	14.45	29.64
3-5 Years	18.78	25.47
5-7 Years	13.64	11.39
7+ Years	34.15	21.26

Rating composition (%)

Rating	Fund	Benchmark
AAA	36.40	78.96
AA	21.82	13.07
A	22.48	5.50
BBB	13.86	1.79
Sub-Investment Grade	4.03	0.09
Not Rated	1.41	0.59

Modified duration

	Years
Fund	2.75
Benchmark	3.41

Notes:

- Returns greater than one year are annualised.
- Past performance is not a reliable indicator of future performance.
- The benchmark to June 1998 was the UBS Semi-Government Bond Index.
- Fund composition tables may not total 100% due to rounding.

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