

Leyland Lines is our monthly newsletter providing investors with our insights on the overall market, individual companies and other relevant issues. All the information contained in this newsletter is for general reading only and should not be taken as a personal recommendation. We encourage you to call Leyland Private Asset Management for specific advice in relation to your portfolio.

Leyland Private Asset Management would like to inform all of our Sydney clients that we have moved.

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Welcome to the March 2009 edition of Leyland Lines

Since our last newsletter the market has fallen and recovered by over 10%. In fact the markets recovered by 15% in just the past 2 weeks. It has been insightful to witness investor sentiment - at exactly the same price points - on the way down as well as on the way up. While there has been a general feeling of relief recently, some investors are now ruing that they may have "missed the bottom".

A very wise man once said "tops and bottoms are made for fools" - amongst the many clichés surrounding investment markets, this is one of the best.

We continue to reiterate that when one purchases a share; one is purchasing a slice of a business and should be unconcerned with short term price movements which are almost always unrelated to the long term fundamentals of the business.

At the moment many investors are enquiring about preference shares (we mentioned SEV Preference Shares recently). Whilst preference shares can be appealing, we would point out that

this is not the time to be afraid and get defensive. Whilst there is no doubt the global economy is in bad shape, this is a unique opportunity to purchase very sound businesses at historically cheap prices...there is a clearing sale on equities at the moment. Additionally, if the global stimulus packages do work, the risk of inflation may become very pronounced. Cash is certainly NOT king when inflation abounds.

In this edition of Leyland Lines we review Sonic Healthcare which many of our clients own. In addition we look at Flexigroup, which has belied its share price by continuing its run of healthy profits whilst the share price has fallen 90% - this is what we would consider de-coupling!

We also revisit gold and review Oz Minerals in light of the recent events.

In the past nine months we have witnessed a plethora of share placements and associated share purchase plans. Our friends at the intelligent investors have kindly submitted their recent article which helps investors filter through SPP's and decide whether or not to participate.

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Sonic Healthcare Limited (SHL)

Sonic Healthcare provides pathology and radiology services in Australia, and around the world. The company led the consolidation of the medical diagnostics sector in Australia in the 1990s and has continued to expand via acquisition into Asia, Europe and the US.

The domestic strategy is to retain cost leadership through the reinvestment of capital into new technology while the international strategy has been to add bolt on acquisitions to form beachhead investment into Europe and the US. These international facilities typically have surplus capacity. So, through improved efficiencies these new sites enable the rationalisation of processing while saving on administration cost via economies of scale and centralisation of processes.

Until very recently Sonics share price has been a stalwart of resistance in a market where many companies around them were imploding.



Full credit must be given to Colin Goldschmidt and his team for keeping disciplined during their acquisition growth strategy which has been occurring consistently over the last 8 years. Sonic has managed to make good acquisitions at fair prices whilst keeping debt at manageable levels. Sonic has also managed to replicate its formula in many different markets and now provide pathology and radiology services in Australia, the UK, US, New Zealand, Germany and Hong Kong. Sonic is currently increasing their presence in Europe and the USA – leveraging off existing operations and making full use of current excess capacity.

Full credit must be given to Colin Goldschmidt and his team for keeping disciplined during their acquisition growth strategy which has been occurring consistently over the last 8 years.

Notwithstanding their acquisitions, Sonic's generic growth in profits is extremely resilient and relatively recession proof.

Sonic Healthcare reported NPAT up 20.5% to \$136.51m for the half-year ended 31 December 2008. Revenue from ordinary activities was \$1.44bn, up 27.7% from the same period last year. Diluted EPS was 38.8 cents compared to 34.7 cents last year. Net operating cash flow was \$187.69m compared to \$174.05m last year.

The interim dividend declared was 22 cents compared with 20 cents last year.

Sonic has really experienced an uncharacteristic fall in share prices, providing investors with a rare opportunity.

Whilst Sonic is not a high profile growth story, it provides defensive earnings with proven management over a long period of time – just what many investors are looking for at the moment.

SHL (\$10.95)	2007A	2008A	2009F	2010F	2011F
EPS (cps)	65.50	73.50	82.90	94.70	104.70
PE (x)	16.72	14.90	13.21	11.56	10.46
DPS (cps)	46.00	52.00	57.00	63.00	70.00
Yield (%)	4.20	4.75	5.21	5.75	6.39
Franking (%)	100.00	100.00	100.00	100.00	100.00

Sources: Aspect Huntley, Credit Suisse, Macquarie Research

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Flexigroup (FXL)

We have written about Flexigroup in the past. It is one of many companies which have fallen by 80-90%, but which now offer significant upside potential over the medium to long term.



Flexigroup provides retail finance at point-of-sale under various brand names including Flexi rent, EzyWay, Flexi way and Certegy Ezipay. They distribute their finance operations in high profile stores such as Harvey Norman and Noel Leeming, and primarily provide finance for medium or larger size purchases.

In the past 24 months, Flexigroup has also undertaken a strategy to diversify their operations into areas such as personal finance and travel finance through larger outlets such as Flight Centre (which we mentioned in our last newsletter). Flexigroup has also been taking advantage of recent world events and have put their relatively strong balance sheet to good use. The recent acquisition of Certegy has proven to be almost prophetic.

Whilst Flexigroup's share price has fallen 93% from a high of \$3.16 to a recent low of 22c, the underlying earnings of the company have shown far more resilience. Flexigroup reported NPAT of \$14.62m (underlying profit of \$16.4m) for the six months ended December 31st 2008, and at the same time reiterated full year profit forecasts of \$28 - \$30m. Flexigroup also paid a 3c fully franked dividend. With a current share price of

Whilst Flexigroup's share price has fallen 93% from a high of \$3.16 to a recent low of 22c, the underlying earnings of the company have shown far more resilience.

40c, Flexigroup's market capitalisation is \$93m, which put Flexigroup on a very undemanding PE multiple of 3.2x forecast earnings.

In an improving economy and investment climate, Flexigroup is likely to benefit from a multiple of both higher earnings and a higher PE multiple. Whilst the downside risk appears quite limited, the upside potential over the medium term is quite significant.

Flexigroup also have solid management and a quality board led by Margaret Jackson.

We believe Flexigroup remains undervalued by the market and provides significant upside potential on a risk/return basis.

FXL (\$0.40)	2007A	2008A	2009F	2010F	2011F
EPS (cps)	16.70	14.80	11.50	13.00	14.50
PE (x)	2.40	2.70	3.48	3.08	2.76
DPS (cps)	5.50	5.50	5.60	5.20	6.00
Yeild (%)	13.75	13.75	14.00	13.00	15.00
Franking (%)	100.00	100.00	100.00	100.00	100.00

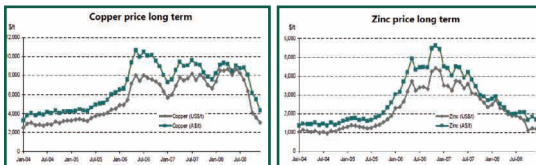
Sources: ABN Amro, Citibank

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OZ Minerals - A fall from grace

Oz Minerals is the result of a merger between cash rich Zinifex and project rich Oxiana. At the time of the merger the company commanded a market capitalisation of \$12 billion making it Australia's third largest diversified miner and the world's second largest zinc producer. OZL also had a significant footprint in the copper, lead, gold and nickel business.

Much has changed since the company's early days. With the corresponding collapses in both the credit markets and the metals markets, OZL saw their project economics turn on them almost over night. Zinc fell from over \$5500 per tonne in 2006 to less than \$1500 per tonne by the end of 2008. Similarly Copper fell from its peak of almost \$11,000 per tonne to \$4000 per tonne by the end of 2008.

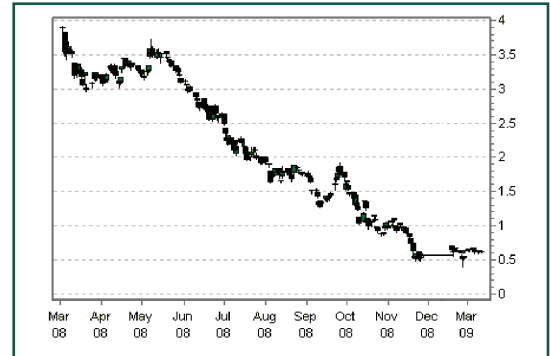


On top of the collapse of their profits and the value of their in-ground reserves, OZL was informed towards the end of 2008 that its line of credit would not be extended as they had expected. Essentially, this meant that their 'long-term debt' (as it was quoted on their balance sheet) suddenly became a short term liability.

Following the announcement that their long term debt was suddenly a short term problem, OZL went into battle to extend their credit on a month-by-month basis. In November 2008 – sighting the ongoing discussions with financiers and the volatile price of their equity - Oz Minerals went into a trading halt (later a suspension) which lasted 3 months.

There have been few falls from grace as spectacular as the former market darling Oxiana (turned OZL)

12 month chart



Minmetals

It certainly seems that Minmetals is offering to under pay for quality assets. However, - as stated by Andrew Michelmore (CEO) - without the offer, the finance companies would have long ago called in their debt and potentially sent OZL into administration.

Minmetals is a state owned Chinese company. Founded in 1950, it is the country's largest base metal trader, mainly engaged in the mining, smelting, production and trade of basic metals and raw materials. It competes with other big state-run traders such as Sinosteel for ongoing state funding and approval.

Aside from the obvious benefits associated with buying quality assets at cheap prices, the purchase of OZL makes sense for Minmentals on several fronts. Two of the most obvious reasons include:

- Surety of supply – in an environment of tight supply, owning the producer gives Minmetals a substantial competitive advantage.
- Gain a foothold into the Australasian resources market – Minmentals can use the OZL 'shell' to acquire further complimentary assets

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OZ Minerals - A fall from grace cont'd

While some pundits have suggested that a state owned company would offer discounts to all Chinese owned entities, to suggest so would be to misunderstand the dynamics of the Chinese - state owned - business world. It is essential to recognise that each state owned company is independent of any other. In fact they are competitors for government favour. It is highly unlikely that Minmetals will sacrifice their profits for the benefit of one of their (state owned) competitors, thereby skewing the competitive nature of the wider industry.

The Offer:

Minmetals has offered to pay 82.5cents per OZL share, and to pay off the outstanding \$1.15 billion of debt.

The Oz Minerals Board of directors strongly recommends accepting the offer in the absence of a better proposal, stating the following benefits:

- The current offer is at a 50% premium to the last OZL price before the bid.
- The current offer is at a significant premium to the current share price.
- The cash bid offers certainty for shareholders
- The current offer secures the business of Oz Minerals (more of a concern for management than for the share holders)

While due diligence has been completed, and the company has the support of OZLs board, both companies continue to wait on regulatory authority before the acquisition can go ahead. While there is always concern regarding foreign states buying local assets, the matter was further complicated as some of Oz Minerals assets are located along military property. As such, there remains some uncertainty regarding the outcome of the FIRB (regulatory) and Treasurers review - due later this month.

The value

Since the company is currently swamped by concerns of near term survival little attention has been granted towards the 'value' of Oz Minerals. Stated in the company's most recent reports - and after massive write downs in asset valuations - the balance sheet states that the businesses equity is worth \$3.23billion, with Net Tangible Assets (NTA) worth \$1.03. These numbers are a huge premium above the current share price and represent a significant premium above the current recommended takeover offer. However in the current environment asset values are difficult to ascertain - an asset is only worth what someone is willing to pay for it; recent movements in commodity prices may even result in an increase in some of the asset values.

The imminent completion of Prominent Hill (the company's premier project) is expected to strengthen cash flow as a result of the new production. If Oz Minerals can find a way to overcome their near term liabilities the business will be in a significantly stronger position than they were just a few short months ago.

While any investment in Oz Minerals today is more about a bet on regulatory approval for the deal than an actual belief in the value of the company itself, for those investors holding OZL, it is comforting to know that profitable projects continue to come on line, unprofitable projects are being delayed or put into care & maintenance, and there is value left in the company despite all the near term troubles they are facing.

We are currently recommending our clients continue to hold OZL in anticipation of governmental approval or a competing offer.

Share price during trading halt	55cents
Current share price	60.5cents
Minmetals Offer	82.5cents
NTA*	\$1.03

* as stated in FY08 report

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As Good as Gold?

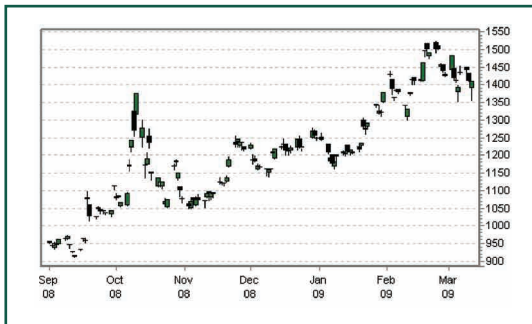
Nothing is as sure as death and taxes, but for as long as anyone can remember, gold has been the universal store of wealth.

In September of last year we visited the topic and discussed the major catalysts that typically move gold. At the time we were most concerned about inflation. After all, with a global food shortage, prices at the markets steadily rising, social unrest on the increase, and peak oil all making front page news; inflation was front and centre in everyone's minds.

Things have changed; deflation and financial uncertainty is the new issue amongst economists, however, as mentioned in our introduction, Governments have taken unprecedented steps to 'stimulate' their way out of a recession – the effects of this on inflation remain to be seen.

So what has this meant for gold?

6 month gold chart



As the graph above illustrates, the current global uncertainty has been great for gold investors.

So let's take another look at the drivers of gold and consider where we can expect things to go from here.

THE THREE CATALYSTS

Since the institution of organised trade, gold has been the store of value that everything else has been measured against.

In modern times there have been three catalysts that have affected the price of gold over the long term.

1. Inflation:

- Seen as a natural hedge against the devaluation of paper money, gold has typically outperformed during prolonged periods of inflation.

2. Risk of financial collapse:

- When sovereign risk appears and there is no "safe currency", gold is often purchased for its universal appeal and recognized for its intrinsic value. As such, when financial markets threaten to collapse, gold has rallied as an alternative investment.

3. The US dollar:

- In modern times gold has been quoted in US dollars. Therefore, when the dollar falls (as it has since 2000) gold tends to appreciate.

As the old brokerage adage goes, past performance does not guarantee future results, but considering the longevity of this correlation, and the commonsense of the relationships, it would seem a prudent to consider these fundamental aspects and their likely effect on gold shares over the medium term.

INFLATION:

As mentioned above, deflation is the new concern for global leaders. However, we believe this to be a minor and short term issue.

Avoiding deflation is easy: inflate. So, while single income families await their \$900 gift from the Labour government, the US run up a multi trillion dollar deficit, and while in England they are discussing 'monetising their debt' (aka creating money out of thin air to buy government bonds), investors can be assured that deflation will be conquered.

Consider that the US currently has interest rates set to zero and that Australia and Europe are likely to reduce interest rates again. There is no doubt that falling prices are what's keeping politicians up at night. There is equally little doubt that once all is said and done we will be left to deal with a 'solution' much worse than the original problem.

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As Good as Gold? cont'd

FINANCIAL COLLAPSE:

Consider the financial environment since June 2007. To mention just a few of the more well known names, we have seen the effective collapse of:

- Indy Mac
- Bear Sterns
- Lehman Brothers

The Nationalisation of:

- Northern rock (UK)
- Fannie Mae and Freddie Mac (USA)
- AIG (USA)

The ongoing wealth destruction from:

- Alco Financial
- Babcock and Brown
- and MFS

And the fear of financial fraud

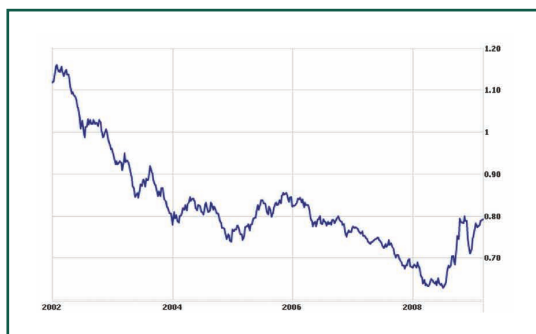
- Bernard Madoff
- Sir Allen Stanford

Clearly the sub-prime crisis coupled with the on going credit crisis has placed much of the global financial market under pressure. So much so that many popular 'bears' have called the entire system into question.

AMERICAN DOLLAR:

Since 2000 the US dollar has depreciated some 40%. Some would argue that this was the result of a weakening American economy, other suggest it is the result of a loose Fed and an increased money supply.

USD vs. Euro



Since July there has been a strong dollar rally. However, this rally has been the result of a total loss of faith in all investment classes. As such, the US dollar has risen as it is perceived as a safe haven. That said the question remains: what will happen to the US dollar once its major current holders and investors (China and Japan) decide to cease supporting a currency that has announced its intention to pay off its debt via inflationary means. Once the inflow from the east stops, many analysts expect to see a recommencement in the long term down trend for the dollar.

THE OUTLOOK:

While no one can be certain of what the market will decide on a day to day basis, an investor can determine the fundamentals of a company (or sector) and base their long term outlook on those expectations.

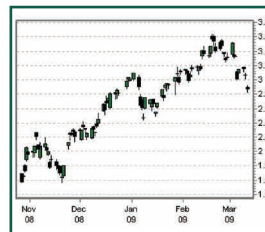
Despite the recent and persistent dollar rally, we believe that all three factors that have historically determined the value of gold continue to paint a very positive picture for the yellow metals medium term outlook.

There is little doubt that regulators will ultimately find a way to deal with the losses in the financial sector. However, -in the short term- there are many question marks around the future of many financial institutions (so much so that short selling them is banned in Australia) In the longer term, the question remains: how will policy makers deal with their solution (inflation), when it too becomes a problem?

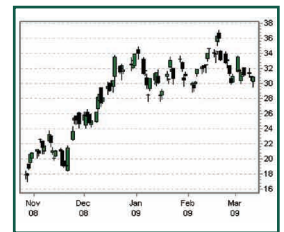
AND SHARES?

Not surprisingly, the two companies we looked at six months ago have done very well.

Lihir Gold



Newcrest Mining



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As Good as Gold? cont'd

However, both seem to be lagging the recovery in physical gold. In March of last year, when gold was selling at AUS\$1000 Newcrest reached \$40.50, while Lihir was as high as \$4.39. Today with Aussie gold at \$1500 (50% higher) Newcrest remains just over \$30 while Lihir are at \$3.

There is no way to know just what the stock market will do, but as gold becomes more mainstream, and investors rush to it to avoid

the global turmoil some analysts are calling for physical gold to return to their inflationary adjusted 1980's high of around US\$2000. Should this be the case, we can expect to see both our gold producers and explorers share prices significantly higher.

In the mean time we continue to watch the events with fascination and increase our positions during genuine corrections.

With the recent spate of Share Purchase Plans, our friends at the intelligent investor have put together this very salient article which we commend to you.

If you would like to know more about the intelligent investors please visit <http://www.intelligentinvestor.com.au>



Profiting from Share Purchase Plans

Westfield's current Stapled Securities Purchase Plan offers a timely lesson in how to profit from share or security purchase plans, even if you don't wish to purchase more securities.

Westfield's current Stapled Securities Purchase Plan (SSPP) provides the perfect opportunity to take our recent Investor's College article – Your guide to retail share offers – for a test run. If you held Westfield securities on 26 February – the record date – you will be entitled to purchase 50, 100, 250 or 498 securities at \$10.04 without paying brokerage costs.

We'll start with the first question in our survival guide – do you wish to buy more securities for the long term? Well, our current recommendation on the company – Long Term Buy – suggests doing just that, so long as it improves the balance of your overall portfolio.

So let's say you decide to purchase 498 securities. Moving across to the second box, Westfield went ex-distribution on 2 February so we can ignore distributions.

But is the purchase plan the best way to buy those securities? At what price would it be cheaper to skip the plan and buy on the market? Purchasing 498 securities at \$10.04 through the plan would cost \$5,000. To calculate the market price you'd need to do better, deduct your brokerage costs from the \$5,000 and divide the total by 498 securities. Brokerage costs of \$30, for example, would leave \$4,970 to spend on securities and you'd need a price of \$9.98 to pick up 498 of them.

Don't rush

The current stock price is \$10.45, which means it's currently wiser to invest through the SSPP than on the market. But don't rush off the paperwork just yet – you have until 31 March to make your decision. Perhaps next week the stock will trade below \$9.98 and you'll find an on-market purchase the more attractive option. With a BPAY® facility available to pay for new securities issued through the SSPP, you can wait until the last moment to decide (and logically you should do just that).

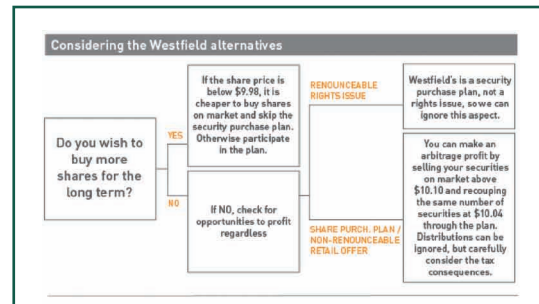
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Profiting from Share Purchase Plans cont'd

For those who choose not to purchase more securities for the long term, the next step is to consider the possibility of arbitrage. At what price could you sell 498 securities, for example, on the market and then replace them through the offer to make a profit? Buying 498 securities through the offer would cost \$4,999.92 and, with brokerage of \$30, you'd need sale proceeds of \$5,029.92 to make a profit. Dividing that by the 498 securities gives \$10.10, which is the price you'd need to make the arbitrage worthwhile – if we ignore tax.

That's a big if, though, and you need to make sure you understand the taxation consequences of your sale and repurchase before acting. As we explained in the Investor's College article,

any arbitrage should be more attractive to those who bought at a higher price than today's, while it might be more marginal for those who bought many years ago at a much lower price. Remember the offer closes on 31 March.



Disclosure: Staff own securities in Westfield, but they don't include the author, Nathan Bell.

Individually Managed Accounts (IMAs) Resources

Leyland Private Asset Management has been running IMAs for over 5 years now. Most share portfolios are balanced with many self managed super funds also being run as an IMA.

The IMA vehicle is the ideal structure, as the client owns the shares. The timing of purchases and weightings in the most suitable sectors is much more efficient than managed funds. Capital gains management and franking credits are also major advantages of the IMA structure.

We believe that history will prove 2009 as a bellweather year for Australian equities. It is

rare that one has the opportunity to purchase so many wonderful businesses at such attractive prices.

Over the long term good quality business models prevail; when those good quality businesses are cheap because of the activities of the lesser quality peers the time is ripe to act.

At Leyland we spend the majority of our time researching investment opportunities on behalf of our clients and believe that this level of dedication is required to achieve satisfactory results.

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