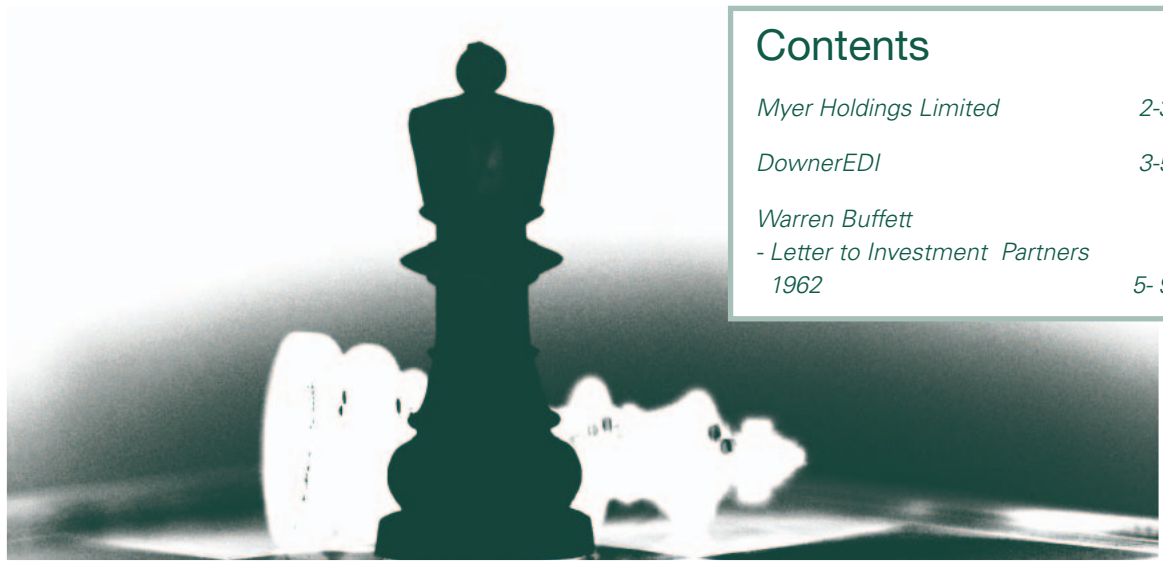


Leyland Lines is our monthly newsletter providing investors with our insights on the overall market, individual companies and other relevant issues. All the information contained in this newsletter is for general reading only and should not be taken as a personal recommendation. Companies and ideas discussed in this newsletter are not necessarily buy or sell recommendations. We don't know when the opportunity to purchase or sell at favourable prices may occur, but when it does we act decisively. For that reason we encourage clients to allow us discretion using our Individually Managed Account service.



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Welcome to the May 2010 edition of Leyland Lines.

The market has been retreating for the last month and is now down approximately twelve percent for the calendar year. The run from 3,700 to 5,048 in nine months was extraordinary, however, at current levels we are starting to see more value in the market. Consider that the market was trading at 4,225 in March 2005.

All Ordinaries 1983 - 2010



Earnings growth has far outstripped share price growth in the past 5-6 years.

As stock pickers we are not necessarily excited by the entire market, in fact, we continue to

avoid many larger companies (particularly in the resource sector).

Our newsletters and comments over the past few months have illustrated that we prefer defensive stocks with sustainable earnings as opposed to companies with presumptive growth factored into the stock price.

In this edition of Leyland Lines we discuss Myer and Downer EDI and although we are not actively buying these companies they are starting to appear on our watch lists.

We also present the latest in our series of letters from Warren Buffett. These are invaluable as the investment techniques of Buffett, Lynch, Templeton and Graham have stood the test of time for the past 100 years and through all manner of bull and bear markets; as Ben Graham says:

"The intelligent investor is likely to need considerable will power to keep from following the crowd."

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Myer Holdings Limited

Myer floated on the ASX in October 2009 at \$4.10 and has disappointed investors since. We mentioned in October that at 16x earnings, Myer was too expensive and we did not participate in the IPO. MYR was also mentioned in the January newsletter, and we revisit it in this edition given continued share price weakness.

Myer Daily Price Chart



Myer recently reported Q3 sales of \$671m, which is flat compared to the previous corresponding period. The reasons given for flat sales were;

- A fall in foot traffic in stores
- Increase in promotional activity
- Underperformance of the Bourke Street store
- Interest rate rises offset the impact of the government stimulus measures

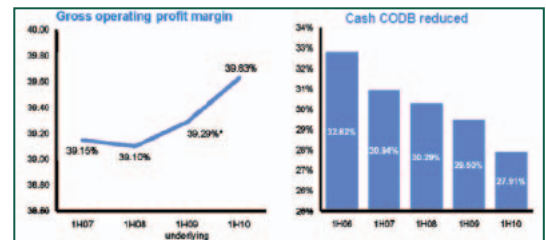
Full year 2010 sales and earnings guidance was re-iterated with sales growth of 1% to 2%, and EBIT growth of 10.7% to \$261 million.

The refurbishment of the Bourke Street store is expected to be completed by Christmas 2010. Bourke Street is currently trading at \$80m below pre-refurbishment levels. The floor-by-floor opening of this store will commence in July. Myer continues to report an uplift of sales from refurbished stores which, combined with the opening of two new stores in the first half of 2011, should positively impact revenues.

Private equity cut back on advertising prior to listing to reduce costs but the effects have been felt since. Promotional offers launched through the Myer One loyalty program are aimed at encouraging customers back to Myer. The Myer One card, which accounts for 60% of total sales, provides valuable customer information allowing for effective marketing and product promotions.

The rollout of CCTV in all stores is underway to reduce theft – otherwise referred to as 'shrinkage.'

Myer was able to maintain margins across all apparel classes. Electronics and cosmetics were the laggards with heavy discounting and deflation. Supply chain initiatives are also aimed at reducing costs and improving margins. Margin improvements are anticipated through direct sourcing of inventory from China.



MYR continued to reduce net debt for the year to \$694m with banking covenants comfortably met.

Discretionary consumption is challenging in the prevailing environment of continued economic uncertainty and rising interest rates. However, as the share price falls, the margin of safety increases; we believe many of the risks are reflected in the discounted share price. Profit growth is clearly not factored into the share price, and MYR continued to lag discretionary peers by ~25% despite offering comparable EPS growth and a higher yield.

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Resource Myer Holdings Limited cont'd

	PE			3 yr EPS (compound)	Yield
	2010	2011	2012		
Myer Holdings Limited	10.1	9.6	8.4	10.50%	6.60%
Billabong International Ltd	18.8	15.1	13.5	15.80%	3.30%
David Jones Limited	13.3	12.4	10.9	10.40%	7.20%
Harvey Norman Holdings	12.2	11.3	10.3	7.90%	4.10%
The Reject Shop Ltd	17.9	15	13.2	13.30%	4.10%

The remainder of 2010 will remain challenging for Myer as the refurbishments and cost out initiatives will contribute to revenues in 2011. However, with 2010 guidance reaffirmed, and many positive catalysts in the pipeline, Myer is the most attractive stock in the retail sector.

Downer EDI

Downer EDI (DOW) consists of a group of companies that focus on infrastructure, rail, telecommunications, mining, engineering, energy and consulting services. The company operates predominantly in Australia, New Zealand, Asia Pacific and the United Kingdom. They have over 24,000 employees, with total assets standing at A\$ 3 billion and an annual turnover of A\$ 5.6 billion.

The company has five main divisions as follows:

Engineering

The EDI Engineering division comprises four core business streams;

- Projects- This includes pre-feasibility and feasibility studies, scoping and design, and engineering procurement and construction management
- Contracting- This involves constructability reviews, high voltage systems, electrical and communications contracting, mechanical contracting, fabrication and shutdowns
- Technical Services- This division deals in telecommunication services, subscription TV, business and consumer technology

(install and repair) and technical facilities management

- Power Systems- This includes generation, transmission lines, substations, distribution and renewable energy

Works

EDI Works is a leading provider of engineering and asset maintenance delivery in the infrastructure sector. Key areas of expertise are building local communities and developing and maintaining customer's infrastructure assets, including network maintenance and management for road, rail and water assets. Customers include federal, state and local governments, public utilities and major private organisations.

Mining

EDI Mining has been providing civil earthmoving and contract mining services for almost 90 years. More specifically, they offer services in coal and metalliferous mining, open-cut and underground mine planning, civil and bulk earthworks, exploration drilling, blasting services and explosives manufacture and supply, crushing services and tyre management.

Leyland Lines

DownerEDI cont'd

Rail

Downer EDI Rail is Australia's largest provider of rolling stock and associated maintenance. It offers services in the design, manufacture, refurbishment, overhaul and maintenance of diesel electric locomotives, electric and diesel multiple units, rail wagons, traction motors, rolling stock and related services.

Consulting

Downer EDI Consulting provides front-end engineering design and consulting capabilities through two subsidiaries:

- CPG- Based in Singapore, CPG is an infrastructure, building development and management services provider with operations reaching the ASEAN region, India, China, South America and the Middle East.
- Snowden- Provides consulting services, technology solutions and technical training to the mining and related sectors and is headquartered in Perth with bases in Brisbane, Johannesburg, London and Bela Horizonte.

Recent Events

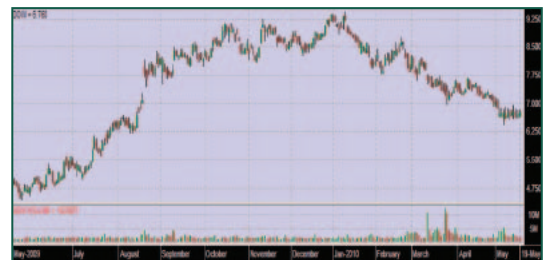
- Downer EDI recently reported first half NPAT of \$87 million, well ahead of consensus forecasts and 2% up on the previous corresponding period. An interim dividend of 13.1 cents per share was declared with no franking.

Divisionally, Engineering revenue declined 15% to \$870 million affected by the increasingly competitive tender environment across resources and LNG markets. Works revenue increased by 3%, largely driven by Australian stimulus-related infrastructure spending. Mining was the standout performer, with EBIT up 73% despite lower revenues and was driven by enhanced operating efficiency and cost reductions. Rail revenue increased 4% and earnings rose 3% supported by resource production growth. This should be supported in the near term

by ongoing demand from freight customers including Asciano, QR and BHP.

- The company flagged financial year NPAT 2010 guidance of 5% growth with the majority of market analysts believing this to be very conservative. They reported a \$16.4 billion order book and, importantly, does not need to win additional contracts to achieve full year earnings guidance.
- Significantly, since reporting, Downer EDI was awarded preferred tender status on a \$3 billion contract with Fortescue Metals Group (FMG) for the provision of mining services at its Christmas Creek operation in Western Australia. This contract is one of, if not the largest mining contract won in Australia this decade and will double EDI Downers mining book to \$5.5 billion. The Mining business currently contributes around \$1 billion of revenue per annum or 17% of total financial year revenue so the inclusion of this contract would be a major fillip for the company.
- This new contract will add diversity to the mining business as they predominantly operate in the Eastern states of Australia at present. Usually, a contract of this size would require substantial capital expenditure however, sub contractors would bear a large amount of the costs and the capital expenditure will gradually ramp up over time, rather than 100% being required at the start of the project.

DOW Daily Price Chart



Leyland Lines

DownerEDI cont'd

Risks to the company:

- The mining and infrastructure booms in Australia hinge on global macro factors, the most significant of which are events in the US and China. Any downturn would almost definitely see Downer EDI's significant pipeline of contracts in all of its divisions severely jeopardised. This in turn would also see very little new business opportunities arise;
- The company's risk management and financial forecasting/control have historically been a weakness;
- The new CEO may take a 'wait and see' approach and delay selling non-core assets;
- The proposed Resources Super Profit Tax (RSPT) could deter mining companies from commencing projects, once again adversely affecting Downer EDI's pipeline of business and new opportunities.

Taking these risks into account, the company's valuation of 11X financial year 2010 earnings is attractive, especially when compared against its peers being Leightons at 16.4X, UGL at 16X and Transfield at 14.2X. With the mining boom still seemingly robust, a strong balance sheet, a quality pipeline of projects, and strong potential for outperformance when considering management's conservative guidance, we believe Downer EDI is to be strongly considered for investors wanting exposure in this sector.

DOW \$6.14	2008 A	2009 A	2010 E	2011 E	2012 E
EPS (cps)	48.31	55.54	58.24	64.28	73.53
PE (x)	12.71	11.05	10.54	9.55	8.35
DPS (cps)	25.50	29.00	42.01	45.67	51.09
Yield (%)	4.15%	4.72%	6.84%	7.44%	8.32%
Franking (%)	0%	0%	0%	50%	75%

Warren Buffett - Letter to Partners - July 1962

A Reminder:

In my letter of January 24, 1962, reporting on 1961 I inserted a section entitled, "And a Prediction." While I have no desire to inflict cruel and unusual punishment upon my readers, nevertheless, a reprinting of that section, in its entirety, may be worthwhile:

And a Prediction:

Regular readers (I may be flattering myself) will feel I have left the tracks when I start talking about predictions. This is one thing from which I have always shied away and I still do in the normal sense.

I am certainly not going to predict what general business or the stock market are going to do in the next year or two since I don't have the faintest idea.

I think you can be quite sure that over the next ten years there are going to be a few years when the general market is plus 20% or 25%, a few when it is minus on the same order, and a majority when it is in between. I haven't any notion as to the sequence in which these will occur, nor do I think it is of any great importance for the long-term investor.

Over any long period of years, I think it likely that the Dow will probably produce something like 5% to 7% per year compounded from a combination of dividends and market value gain. Despite

the experience of recent years, anyone expecting substantially better than that from the general market probably faces disappointment.

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Warren Buffett - Letter to Partners - July 1962 cont'd

Our job is to pile up yearly advantages over the performance of the Dow without worrying too much about whether the absolute results in a given year are a plus or a minus. I would consider a year in which we were down 15% and the Dow declined 25% to be much superior to a year when both the partnership and the Dow advanced 20%. I have stressed this point in talking with partners and have watched them nod their heads with varying degrees of enthusiasm.

It is most important to me that you fully understand my reasoning in this regard and agree with me not only in your cerebral regions, but also down in the pit of your stomach.

For the reasons outlined in my method of operation, our best years relative to the Dow are likely to be in declining or static markets. Therefore, the advantage we seek will probably come in sharply varying amounts. There are bound to be years when we are surpassed by the Dow, but if over a long period we can average ten percentage points per year better than it, I will feel the results have been satisfactory.

Specifically, if the market should be down 35% or 40% in a year (and I feel this has a high probability of occurring one year in the next ten—no one knows which one), we should be down only 15% or 20%. If it is more or less unchanged during the year, we would hope to be up about ten percentage points. If it is up 20% or more, we would struggle to be up as much. The consequence of performance such as this over a period of years would mean that if the Dow produces a 5% to 7% per year over-all gain compounded, I would hope our results might be 15% to 17% per year.

The above expectations may sound somewhat rash, and there is no question but that they may appear very much so when viewed from the vantage point of 1965 or 1970. It may turn out that I am completely wrong. However, I feel the partners are certainly entitled to know what I am thinking in this regard even though the nature

To invest successfully over a lifetime does not require a stratospheric IQ, unusual business insights, or inside information. What's needed is a sound intellectual framework for making decisions and the ability to keep emotions from corroding that framework.

Warren E. Buffett

of the business is such as to introduce a high probability of error in such expectations. In any one year, the variations may be quite substantial. This happened in 1961, but fortunately the variation was on the pleasant side. They won't all be!

The First Half of 1962:

Between yearend 1961 and June 30, 1962, the Dow declined from 731.14 to 561.28. If one had owned the Dow during this period, dividends of approximately \$11.00 would have been received so that over-all a loss of 21.7% would have been the result of investing in the Dow. For the statistical minded, Appendix A gives the results of the Dow by years since formation of the predecessor partnerships.

As stated above, a declining Dow gives us our chance to shine and pile up the percentage advantages which, coupled with only an average performance during advancing markets, will give us quite satisfactory long-term results. Our target is an approximately ½% decline for each 1% decline in the Dow and if achieved, means we have a considerably more conservative vehicle for investment in stocks than practically any alternative.

As outlined in Appendix B, showing combined predecessor partnership results, during the first half of 1962 we had one of the best periods in our history, achieving a minus 7.5% result

Leyland Lines

Warren Buffett - Letter to Partners - July 1962 cont'd

before payments to partners, compared to the minus 21.7% over-all result on the Dow. This 14.2 percentage points advantage can be expected to widen during the second half if the decline in the general market continues, but will probably narrow should the market turn upward. Please keep in mind my continuing admonition that six-months' or even one-year's results are not to be taken too seriously. Short periods of measurement exaggerate chance fluctuations in performance. While circumstances contributed to an unusually good first half, there are bound to be periods when we do relatively poorly. The figures for our performance involve no change in the valuation of our controlling interest in Dempster Mill Manufacturing Company, although developments in recent months point toward a probably higher realization.

Investment Companies During the First Half:

Past letters have stressed our belief that the Dow is no pushover as a yardstick for investment performance. To the extent that funds are invested in common stocks, whether the manner of investment be through investment companies, investment counselors, bank trust departments, or do-it-yourself, our belief is that the overwhelming majority will achieve results roughly comparable to the Dow. Our opinion is that the deviations from the Dow are much more likely to be toward a poorer performance than a superior one.

To illustrate this point, we have continually measured the Dow and limited partners' results against the two largest open-end investment companies (mutual funds) following a program of common stock investment and the two largest closed-end investment companies. The tabulation in Appendix C shows the five-years' results, and you will note the figures are extraordinarily close to those of the Dow. These companies have total assets of about \$3.5 billion.

In the interest of getting this letter out promptly, we are mailing it before results are available for the closed-end companies. However, the two mutual funds both did poorer than the Dow, with

Massachusetts Investors Trust having a minus 23% over-all performance, and Investors Stock Fund realizing a minus 25.4%. This is not unusual as witness the lead article in the WALL STREET JOURNAL of June 13, 1962, headed "Funds vs. Market." Of the 17 large common stock funds studied, every one had a record poorer than the Dow from the peak on the Dow of 734, to the date of the article, although in some cases the margin of inferiority was minor.

Particularly hard hit in the first half were the so-called "growth" funds which, almost without exception, were down considerably more than the Dow. The three large "growth" (the quotation marks are more applicable now) funds with the best record in the preceding few years, Fidelity Capital Fund, Putnam Growth Fund, and Wellington Equity Fund averaged an over-all minus 32.3% for the first half. It is only fair to point out that because of their excellent records in 1959-61, their over-all performance to date is still better than average, as it may well be in the future. Ironically, however, this earlier superior performance had caused such a rush of new investors to come to them that the poor performance this year was experienced by very many more holders than enjoyed the excellent performance of earlier years. This experience tends to confirm my hypothesis that investment performance must be judged over a period of time with such a period including both advancing and declining markets. There will continue to be both; a point perhaps better understood now than six months ago.

In outlining the results of investment companies, I do so not because we operate in a manner comparable to them or because our investments are similar to theirs. It is done because such funds represent a public batting average of professional, highly-paid investment management handling a very significant \$20 billion of securities. Such management, I believe, is typical of management handling even larger sums. As an alternative to an interest in the partnership, I believe it reasonable to assume that many partners would have investments managed similarly.

Leyland Lines

Warren Buffett - Letter to Partners - July 1962 cont'd

Asset Values:

The above calculations of results are before allocation to the General Partner and monthly payments to partners. Of course, whenever the over-all results for the year are not plus 6% on a market value basis (with deficiencies carried forward) there is no allocation to the General Partner. Therefore, non-withdrawing partners have had a decrease in their market value equity during the first six months of 7.5% and partner who have withdrawn at the rate of 6% per annum have had a decrease in their market value equity during the first half of 10.5%. Should our results for the year be less than plus 6% (and unless there should be a material advance in the Dow, this is very probable) partners receiving monthly payments will have a decrease in their market value equity at December 31, 1962. This means that monthly payments at 6% on this new market equity next year will be on a proportionately reduced basis. For example, if our results were an over-all minus 7% for the year, a partner receiving monthly payments who had a market value interest of \$100,000 on January 1, 1962, would have an equity at December 31, 1962 of \$87,000. This reduction would arise from the minus 7% result, or \$7,000 plus monthly payments of \$500 for an additional \$6,000. Thus, with \$87,000 of market equity on January 1, 1963, monthly payments next year would be \$435.00.

None of the above, of course, has any applicability to advance payments received during 1962 which do not participate in profits or losses, but earn a straight 6%.

Year-end Amendments:

All partners have the right to withdraw or add any amount (rounded to even \$100's) at yearend. This year we hope to get this tended to earlier with the material sent out in October with the right of amendment of intentions any time up to December 31st. This should minimize the December paper flurry.

Our attorneys have advised us to admit no more than a dozen new partners (several of whom have already expressed their desire) and accordingly we have increased the minimum amount for new names to \$100,000. This is a necessary step to avoid a more cumbersome method of operation.

I will close with my usual request that should anything at all in this letter not be clear to you, please be sure to let me hear from you. During July and August I expect to be in the metropolitan New York area except for a trip or two back to Omaha. Therefore, you can get in touch with me either through our office in the Kiewit Plaza, or more directly, in care of Tweedy, Browne & Reilly, 52 Wall Street, New York 5, N.Y.

Cordially,

Warren E. Buffett

APPENDIX A

Dow-Jones Industrial Average

Year	Closing Dow	Change for Year	Dow Dividend	Over-all Result from Dow	Percentage Result
1956	499.47	-	-	-	-
1957	435.69	-63.78	21.61	-42.17	-8.40%
1958	583.65	147.96	20	167.96	38.50%
1959	679.36	95.71	20.74	116.45	20.00%
1960	615.89	-63.47	21.36	-42.11	-6.20%
1961	731.14	115.25	22.61	137.86	22.40%
6/30/1962	561.28	-169.86	11.00 Est	-158.86	-21.70%

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APPENDIX B

Partnership Performance

Year	Partnership Results (1)	Limited Partners' Results (2)
1957	10.40%	9.30%
1958	40.90%	32.20%
1959	25.90%	20.90%
1960	22.80%	18.60%
1961	45.90%	35.90%
6/30/1962	-7.50%	-7.50%

- (1) For 1957-61 consists of combined results of all predecessor limited partnerships operating throughout entire year after all expenses but before distributions to partners or allocations to the general partners.
- (2) For 1957-61 computed on basis of preceding column of partnership results allowing for allocation to general partner based upon present partnership agreement.

APPENDIX C

Yearly Results

Year	Mass. Inv. Trust (1)	Investors Stock (1)	Lehman (2)	Tri-Cont. (2)
1957	-11.40%	-12.40%	-11.40%	-2.40%
1958	42.70%	47.50%	40.80%	33.20%
1959	9.00%	10.30%	8.10%	8.40%
1960	-1.00%	-0.60%	2.50%	2.80%
1961	25.60%	24.90%	23.60%	22.50%
6/30/1962	-23.00%	-25.40%	N.A.	N.A.

- (1) Computed from changes in asset value plus any distributions to holders of record during year.
- (2) From Moody's Bank & Finance Manual - 1962.

Cumulative Results

Year	Mass. Inv. Trust	Investors Stock	Lehman	Tri-Cont.	Dow	Limited Partners
1957	-11.40%	-12.40%	-11.40%	-2.40%	-8.40%	9.30%
1958	26.40%	29.20%	24.70%	30.00%	26.90%	44.50%
1959	37.80%	42.50%	34.80%	40.90%	52.30%	74.70%
1960	36.40%	41.60%	38.20%	44.80%	42.90%	107.20%
1961	71.30%	76.90%	70.80%	77.40%	74.90%	181.60%
6/30/1962	31.90%	32.00%	N.A.	N.A.	37.00%	160.50%

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