NORTHSTAR

ASSET MANAGEMENT

Client Letter 22 October 2008

Quarter End: 30th September 2008

Dear Investor

In the third quarter of 2008, the Johannesburg Securities Exchange (JSE) All Share Index (ALSI) declined by -21.6%. In the same period Northstar's clients' portfolios fell by well less than half that amount. In the past year the JSE ALSI lost -20.4%, and again our clients' portfolios recorded single digit losses.

That we have been able to avoid the carnage that many investors have experienced in their investment portfolios, is attributable to our having positioned our clients' portfolios in defensive companies with transparent and highly predictable future earnings. When compared to the overall market, the companies in which our clients are invested have experienced a significantly more moderate markdown in their share prices. Moreover, this decline will be more easily reversed when contrasted to those worse affected companies whose earnings, we have long argued, were abnormally and unsustainably high.

Clients may also be aware that, subsequent to the reporting period ended 30 September 2008 referred to herein, there has been further volatility in global financial markets. As before, Northstar's clients remain protected from the worst of the losses and their portfolios continue to outperform the overall market.

Despite these losses it may be somewhat reassuring to note that Northstar's track record of outperformance remains intact. Of the 68 general equity investment funds reporting in SA, Northstar's results would make it the sole investment manager to hold a top five position over the 1, 3 and 5 year reporting periods.

While losses are unpleasant to experience and report, as professional investors, we accept them as an occasional and lesser component of the market cycle. Longstanding clients will know that, through our empirical research and the implementation of our investment philosophy, we have consistently outperformed the market in both the up and down legs of the market cycle. This has ensured that we have been able to deliver greater than market returns at lower than market risk and, in so doing, have had the privilege to significantly grow our clients' wealth and look forward to continuing to do so in the years ahead.

Yours sincerely

Alexander Otten

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NORTHSTAR ASSET MANAGEMENT (PTY) LTD.
4 Chester Drive Bishopscourt 7708 South Africa
Tel: 021- 797 8184 Fax: 021- 797 4706
email: info@northstar.co.za web address: www.northstar.co.za

Company registration number 1996/001423/07
VAT registration number 429 01 666 46
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NORTHSTAR

Asset Management

Market Report 22 October 2008

Quarter End: 30th September 2008

The past few months in the global financial markets constitute one of those rare periods when the word 'unprecedented' warrants use.

The recent volatility in prices, both down and up, has been truly unprecedented. We witnessed the widely followed Standard and Poor's index of the top 500 US companies suffer its worst weekly fall since its inception a century ago. This was followed by its largest ever one day price rise. There are similar tales to be told of stockmarkets across the globe.

US Standard & Poor's 500 Stock Index - Historic PE ratio 1985 to present

Source: DataStream International / IBES / Credit Suisse Research

This extreme volatility in prices was not restricted to the share markets for, in the past months, commodities such as gold and oil have seen both their largest ever one day price declines; and, greatest ever one day price gains.

A confluence of factors, most related to the debt or credit markets and the deleveraging of over-geared institutions, led to a cascade of selling which overwhelmed the private capital markets.

Over-borrowed companies needed to deleverage their balance sheets. This can be done either through the sale of assets to reduce debt; or the raising of capital to realign debt ratios. Either way, deleveraging essentially exchanges debt for equity.

The magnitude of assets being sold off swamped the markets. Compounded by the absence of marginal private buyers, this led to prices collapsing which, in turn, caused debt ratios to spiral.

Some participants panicked as they perceived the apparent unravelling of the global financial system. The only buyers capable of breaking the logjam, by removing the overhang through the use of state funding, were national governments. In coordinating their intervention, they were able to neutralise the much feared systemic risks of a global financial markets meltdown.

The unwind will take time. There will be casualties and there will be winners. This process of 'creative destruction' will leave the financial system in better shape than it was and will set the foundation for the subsequent recovery.

We have frequently stated our view that company earnings and profits were at abnormally, and unsustainably, elevated levels. Moreover, we noted that investors were paying premium prices for each unit of these inflated earnings. For many companies their share price was doubly high. The recent market decline has pre-empted the significantly lower earnings which companies will report in the quarters ahead.

On the basis of historic earnings, share prices in the US, and globally, are at 20 year low valuations. However, if one pencils in a 40% decline in US company earnings, then the stockmarket may have a little further to fall before it reaches average, or cheap, valuation levels.

Having thus far fallen by around 40%, further declines will take the market deeper into value territory.

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Northstar has shepherded clients' money in, and through, very tough markets before. In both 1998 and 2002 the stockmarket fell, much as now, by around 40%.

In both of the previous stockmarket declines of 1998 and 2002 our clients, as now, lost significantly less than the losses produced by the overall market. Interestingly, in this past quarter of 2008, we delivered one of our largest ever quarterly outperformance of the Johannesburg Securities Exchange (JSE) All Share Index (ALSI).

In the depth of the Emerging Market Crises of 1998 and the Market Crash of 2002, as now, it was not obvious how the problems would be resolved and what the future would hold.

As the Nobel laureate US economist John Kenneth Galbraith succinctly puts it: “There are two kinds of forecasters: those who don’t know, and those who don’t know they don’t know.”

The final stage of a market decline is always marked with unremitting pessimism as participants despair at how the vicious cycle will be interrupted .

It is at this stage, when forced sellers are dumping and buyers are fearful, that assets can be acquired at deep discounts to their intrinsic value and at prices which reflect dire pessimism and bleak future prospects. However, over time, things usually work out considerably better than those asset prices imply.

Now is a time to dust off and repeat Warren Buffet's classic observation that, to be a successful investor: "One must be fearful when others are greedy, and greedy when others are fearful".

Regular readers of our Market Reports will recall that for the past year, when share prices and markets were peaking, and pricing in a great deal of optimism, we were rotating our clients' portfolios away from those sectors and companies which were at that time 'hot', and towards the stable and defensive.

Many good, and even the great, companies have seen their share price marked down in sympathy with the overall market decline. However, while some companies will feel little impact from the economic slowdown, we are going to see vast downward revisions in the earnings of others. Naturally this will determine how quickly the share price of the respective companies recover and will provide rich opportunities for astute investors.

Many market commentators, usually after the event, are willing to offer detailed explanations for sudden and dramatic moves in financial markets. At Northstar we have little confidence in our, or anyone else's, ability to predict market behaviour. However, we are confident that our ongoing proprietal research, along with the consistent application of our value based investment philosophy, will ensure that, more often than not, the result of these sudden market shifts will be favourable for our clients.

This is because, ultimately, share prices must return to their true intrinsic value and that is the end product of periods of high volatility, such as we are experiencing at present.

As this last quarter has shown, at times such as these, it matters more than ever how one approaches and invests in the financial markets. Share selection has, and will, substantially determine both short-term wealth preservation and long-term wealth creation.

By having avoided two-thirds of the losses that the market delivered in the last year, Northstar has retained the vast majority of the outperformance that we accumulated and compounded for our clients over the past decade.

It is worth reminding ourselves that large fortunes are built on low prices and small fortunes on high prices. We look forward to taking advantage of the prevailing low prices to continue building our clients' fortunes in the years ahead.