

QUARTERLY
REPORT
31 DECEMBER 2009



ORBIS MIS
ORBIS/SM AUSTRALIA
EQUITY

ORBIS/SM AUSTRALIA EQUITY FUND

INVESTMENT OBJECTIVE

The Investment Manager seeks long-term returns for investors that are higher than those of the S&P/ASX 300 Accumulation Index.

INVESTMENT APPROACH

The Investment Manager's basic investment philosophy is the belief that, while stockmarket prices are the best indicator of value for companies over very long periods of time, substantial deviations of those prices from their true value do occur over the short to medium term. Most businesses (and thus their underlying value) do not change much from one week to the next. Yet, their stock prices may be subject to large deviations, often for no particularly good reason.

Accordingly, the Investment Manager's focus is to look for companies whose share price is much lower than what its underlying value suggests it should be, based on the Investment Manager's determination of each company's long-term business fundamentals. The Fund's portfolio is constructed using the "best" of such companies. The Investment Manager relies on the market eventually recognising a company's true value. When the Investment Manager believes this has occurred, it will replace that company with another company which it considers to be undervalued/underpriced by the market at that time.

NOTICES

Buy/Sell Spread. *The Buy/Sell Spread is 0.35%. It represents the estimate of the cost of acquiring (Buy Spread) or disposing of securities (Sell Spread) in the Fund.*

Source. *The source for the S&P/ASX 300 Accumulation Index is Standard & Poor's. ASX 300 is the trademark of ASX Operations Pty Limited ("ASXO"); "S&P/ASX300™" exists pursuant to an arrangement between ASXO and Standard & Poor's (S&P™ is a trademark of Standard & Poor's, a division of The McGraw-Hill Companies, Inc.).*

Returns. *Fund returns are gross of all income, net of all expenses and fees, assume reinvestment of distributions and exclude any spreads that might be payable on some transactions, i.e. on a "mid-to-mid" basis.*

Risk Warnings. *Past performance is not indicative of future performance. The Fund's unit price will fluctuate and the Fund's performance is not guaranteed. When making an investment in the Fund, an investor's capital is at risk.*

Other. *Equity Trustees Limited AFSL No. 240975 is the issuer of units in the Orbis/SM Australia Equity Fund (the "Fund") and Orbis Investment Management (Australia) Pty Limited AFSL No. 298487 is the Fund's Investment Manager. The Fund's Product Disclosure Statement ("PDS") is available from www.orbisfunds.com.au or by contacting Orbis' Client Services Team on +61 (0)2 82248600. You should consider the PDS in deciding whether to acquire, or to continue to hold, units in the Fund.*

This report is not an offer to sell, or a solicitation to buy, units in the Fund. Where the report provides commentary on a particular security, it is done to demonstrate the reasons why we have or have not dealt in the particular security for the Fund. It is not intended to be, or should be construed as, financial product advice. This report is current as at its date of publication, is given in good faith and has been derived from sources believed to be reliable and accurate. It does not take into account your individual objectives, financial situation or needs. Any implied figures or estimates are subject to assumptions, risks and uncertainties. Actual figures may differ materially and you are cautioned not to place undue reliance on such information. Subject to applicable law, we do not provide any warranty of accuracy or reliability in relation to information in this report or accept any liability to any person who relies on it.

ORBIS/SM AUSTRALIA EQUITY FUND AT 31 DECEMBER 2009

Total Rate of Return in Australian dollars	From Public Launch on 4 May 2006		Latest		From 30 Jun 2009	Latest Quarter
	% Annualised		3 Years	1 Year		
Orbis/SM Australia	4.1	0.5	55.1		30.9	0.2
S&P/ASX 300 Accumulation Index	2.6	(0.8)	37.6		25.7	3.4
Relative Performance	1.5	1.3	12.7		4.1	(3.1)

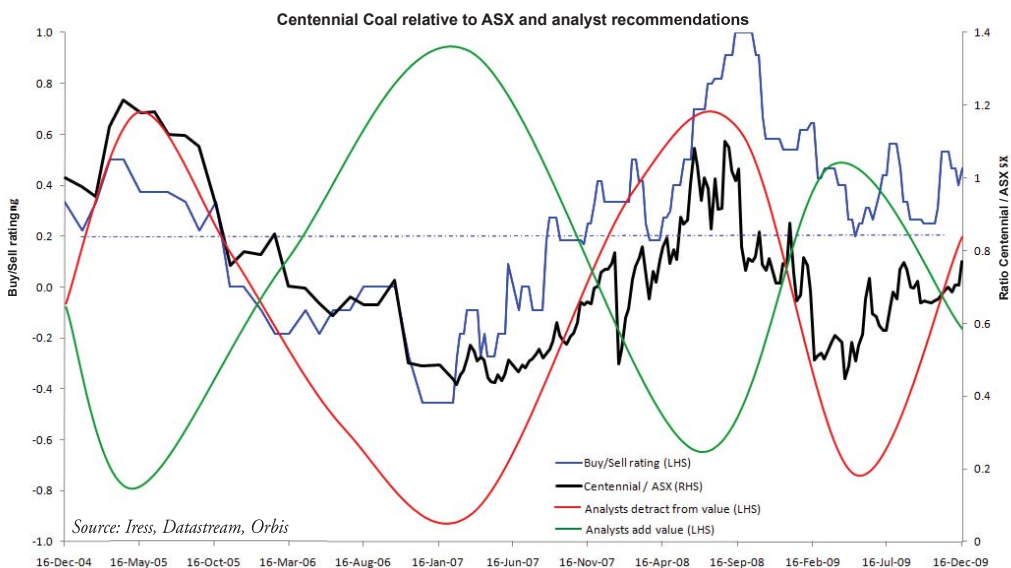
What a year this has been! After a desperately poor start for the Fund in 2009, we managed to end the year with some satisfaction. Hopefully, 2010 will prove to be less exciting.

We often refer to the fact that we are contrarian and therefore tend to buy shares that are disliked by market analysts and commentators. Many clients find this surprising and I have to admit that when I joined the fund management industry (from being a physicist) it took me a while to accept this as reasonable, let alone smart.

If you want to build a bridge and 99% of structural engineering reports tell you the bridge is likely to fall down, you would be well advised not to proceed with the design. The same is true in law – few of us would do something that is explicitly against the advice of our lawyer. One would expect this to be true for investment advice. Highly-rated investment analysts and advisors earn amongst the highest salaries of any profession and attract some of the best minds. Surely their advice should be worth something.

To examine this, we picked Centennial Coal, the share with the largest average weight in the Fund since inception, as a case study. The graph below shows Centennial’s share price relative to that of the stockmarket (indexed to 1). As is clear from the graph, Centennial has had some pretty dramatic periods of out- and under-performance allowing ample opportunity for analysts to add value.

To see what the ‘average’ analyst thought of Centennial over time, we took the number of ‘Buy’ recommendations on the stock, subtracted the number of ‘Sell’ recommendations and divided the answer by the total number of analysts covering the share to arrive at a ‘Buy/Sell rating’. A Buy/Sell rating of zero thus means that the number of analysts that like and dislike the share is the same, while a reading of 0.5 could indicate that there were three out of four analysts recommending a ‘Buy’ and one recommending a ‘Sell’: $(3-1)/4 = 0.5$. Given the natural bias of analysts to be bullish (it is good for their business), the long-term average reading on this score is around 0.2.

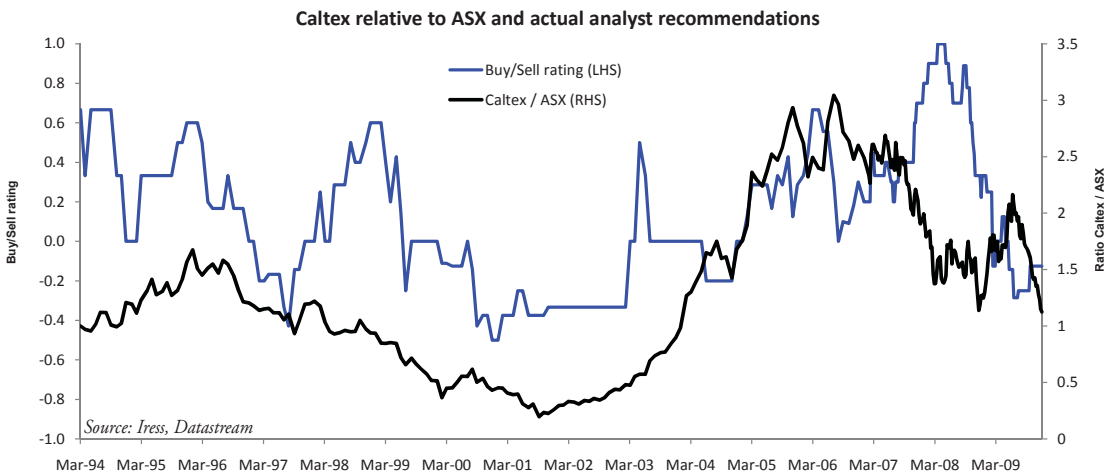


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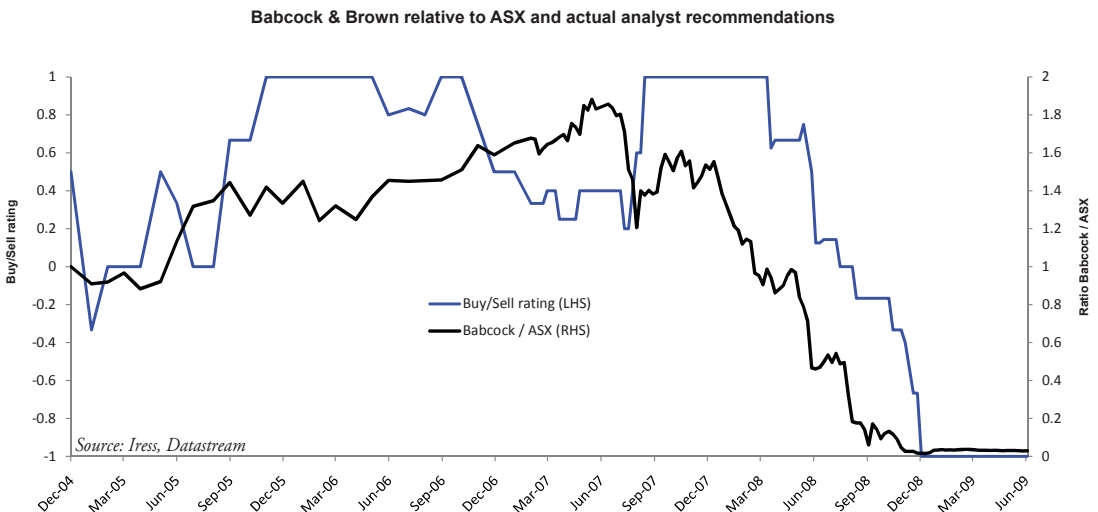
If analysts were good at recommending shares, you would expect the average recommendation to look something like the green line on the previous page's graph with a positive recommendation when the share offered great value (2007) and a net sell bias around major peaks (early 2005 and mid 2008). If analysts were worse than random at predicting what would happen, you would expect to see something like the red line with Sell recommendations dominating near troughs and Buys dominating near peaks.

What really happened is shown by the solid blue line in the graph on the previous page. The average Buy/Sell recommendation (blue line) looks a lot more like the red line than the green line and one can do the mathematics if you need further convincing. In the case of Centennial, you would have done best by carefully listening to the analysts that follow the share, seeing when they reached consensus and then doing exactly the opposite.

Centennial may be a special case where analysts have been unlucky. But below is the same graph for Caltex, currently the Fund's largest holding. The same applies. When Caltex was really cheap in the early part of the decade, it was widely disliked. This really only changed once Caltex went up tenfold off its low with a significant net Buy recommendation in 2006 when the share price was well over \$20.



Another test may be to see whether the analyst recommendations provided any warnings about impending disasters. Few companies have had a bigger fall from grace than Babcock & Brown. In retrospect, it is clear that it was a house of cards, but it is interesting to see how many analysts gave investors a fair warning about the company.



Again the answer is not exactly heart warming. From the middle of 2007 until April 2008, the period when the first cracks in B&B started to appear, each of the nine analysts on record had the company as a 'Buy'. By the time the first 'brave' soul changed his/her recommendation, the stock had already lost more than half of its value. The majority of analysts did not warn investors to sell until B&B was down by more than 90% off its peak and within a few months of being suspended.

One may blame the analysts and call for this seemingly less than useless bunch to be sacked (or worse). But it is the nature of market pricing, rather than the quality of the analysts, that is the problem. The laws governing engineering problems like our original problem of building a bridge are fixed by nature. Proper analysis by experts understanding these laws leads to answers that all experts agree on and that nature also accepts as correct. But the pricing of a share is not fixed by any external laws. The price of an investment is that point where the buyers and sellers at any moment are in balance. Even if everyone improved the quality of their analysis, this will still be the case. The market will simply become more efficient, but buyers will still match sellers. The 'average' analyst can thus never really add value.

But why are they wrong, rather than merely random? We believe this is because of the ingrained practice of listening to the advice of experts every day. If the majority of the 'experts' like a share, buyers will become more confident and sellers less likely to sell. Also, nobody cares more about the opinion of the experts than the experts themselves. As buyers start to dominate, an analyst can risk his lucrative career with a strong contrary opinion. The share price will increase to a point where the buying pressure is only matched by sellers who will accept a very high price as compensation for letting go of something where the outlook and news flow is highly positive. But from this level, it is difficult for things to get better and any unexpected bad news can lead to very big falls. The opposite is true when investors become very pessimistic.

Investors in the Fund will thus often find themselves reading very negative press reports about some of the shares in the Fund with 'experts' vilifying the company and its outlook. That should really make us all feel good, as once a share is widely hated, it is unlikely that things can get much worse. But any good news (or even absence of further bad news) can lead to big upside.

For more than three years, the Fund has had a substantial investment in Centennial Coal. Things are now going very well for the company, the outlook is rosy and analysts recommending it as a buy outnumber those recommending it as a sell. Consequently, we have taken profits on the share and sold the Fund's entire holding during the fourth quarter.

The money has been deployed into Caltex, which is suffering from very low refining margins, has recently had a potential merger declined by the Competition Commission and is more hated than liked by analysts (the Buy/Sell rating in the second graph is currently below zero). We also see the problems, but current prices extrapolate these tough conditions indefinitely. We believe it likely that at some time in the future, things will become more normal and at that point the Fund's investment will yield great returns. In the meantime, our analysis leaves us confident that Caltex will survive these lean times and (unlike B&B) will still be there when things turn.

Yours sincerely,



Simon C Marais

Sydney, Australia
8 January 2010

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STATEMENT OF NET ASSETS (UNAUDITED)

Security	Market Value A\$ 000's	% of Fund
Caltex Australia	39,840	8
Hastings Diversified Utilities Fund	29,809	6
Iluka Resources	22,198	4
PaperlinX	21,677	4
PMP	18,747	4
Australia and New Zealand Banking Group	18,514	4
SP AusNet	18,390	4
National Australia Bank	16,977	3
Australand Property Group	16,543	3
Roc Oil	16,015	3
ALE Property Group	15,525	3
APN News & Media	14,955	3
Pharmaxis	13,646	3
Fisher & Paykel Appliances	13,280	3
Nuplex Industries	12,455	2
Tower	12,381	2
Salmat	12,061	2
Acrux	11,838	2
Valad Property Group	10,376	2
ChemGenex Pharmaceuticals - Ordinary and Options	9,937	2
ING Industrial Fund	9,764	2
Air New Zealand	9,625	2
Centro Retail Trust	9,559	2
Suncorp-Metway	9,484	2
Guinness Peat Group - CDI	8,126	2
Sunland Group	7,504	1
Ridley	7,495	1
Tassal Group	5,634	1
Macquarie Office Trust	5,455	1
Thakral	5,424	1
Positions less than 1%	84,153	16
Total Equity Exposure	507,387	98
Stock Index Futures Bought*:		
SPI 200 03/2010	7,787	1
Net Current Assets	5,025	1
Net Assets	520,199	100
Net Asset Value per Unit	A\$ 1.0898	
Total Assets Under Management for the Australian equity strategy (000's)**	A\$ 1,408,844	

* All stock index futures are fully backed by cash holdings.

** Orbis Investment Management (Australia) Pty Limited also manages several segregated accounts that have the same investment goals and restrictions as the Fund.

CHARACTERISTICS OF ORBIS/SM AUSTRALIA EQUITY FUND

Investment objective	The Fund seeks long-term returns for investors that are higher than the S&P/ASX 300 Accumulation Index (" Benchmark ").
Investments	The Fund is designed to remain continuously invested in selected Australian equities. These equities are selected using extensive proprietary investment research undertaken by the Investment Manager.
Structure	Registered Managed Investment Scheme aimed at Australian investors.
Who should invest?	Investors with a long-term horizon and able to withstand periods of disappointing performance. The Fund's portfolio may deviate meaningfully from its Benchmark in pursuit of superior returns.
Minimum initial investment	A\$50,000. Subsequent minimum investments of A\$10,000.
Minimum Redemption	A\$10,000, subject to maintaining an investment balance of A\$50,000.
Dealing Days	Weekly, normally each Thursday.
Dealing deadlines	<p>Application forms must be received by 2:00 p.m. Sydney time (the "Deadline") on a Dealing Day for processing on that Dealing Day, provided sufficient cleared funds and all applicable customer identification documents have also been received by the Deadline.</p> <p>Redemption requests must be received by 2:00 p.m. Sydney time on a Dealing Day for processing on that Dealing Day. A Unitholder who submits a request for a Significant Redemption must make that request by 2:00 p.m. on the day that is 10 Business Days before the Dealing Day.</p>
Fees and expenses	The Management Fees payable from the Fund have a fixed component (the " Base Fee ") and a performance component (the " Performance Fee "). The Base Fee is 0.75% per annum of the Net Asset Value of the Fund. The Performance Fee is 20% of the extent to which the Fund outperforms its Benchmark once the Fund has reached a new High Water Mark. Other expenses such as stamp duty and GST will be deducted from the Fund as appropriate.



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