# LinQ Resources Fund

## December 2008 Quarterly Investment Update

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# A word from your manager

LinQ Capital Limited ABN 66 098 197 258, your Manager of the LinQ Resources Fund ARSN 108 168 190 (the "Fund"), is pleased to announce the following for the December Quarter 2008:

- The market volatility in the resources sector and in the equities sector globally was extraordinarily high during the last quarter. In light of this, the Fund has been very active selling down positions and continued to actively manage its portfolio for diversification of risk and optimisation of returns.
- Given these market circumstances, the Fund has focussed on investing in high yielding structured investment opportunities that provide some downside risk mitigation whilst maintaining equity upside participation. This is one of the Fund's key differentiating advantages and has proved to be very successful in similar market circumstances in the past.
- The Fund's weighting to established producers has increased, reflecting the Fund's view that many of these producers are significantly under valued in the current market.
- The Fund remains well positioned with its cash to take advantage of investment opportunities in the current market and remains debt free.
- The first of the bi-annual off-market buybacks was triggered in November 2008 representing an 81% premium to the unit price that day. Only 39% of unit holders took this up.

## Overview

The December quarter ended with the global financial system in the midst of turmoil unlike any experienced in our lifetime. The effects of the financial maelstrom have begun to impact the wider economy with global job losses in the December quarter and growth in advanced economies predicted to decline in 2009. Whilst the impact on global economies has been and continues to be substantial, it is predicted by the IMF that global growth will remain positive in 2009 and that key Asian and developing economies will continue to grow in 2009, albeit at a slower rate.

Whilst the global financial system has entered into uncharted territory we have also seen unprecedented action by governments worldwide to stem the crises. This has seen the US Government's Troubled Asset Relief Program inject US$350b into the financial system with an equal amount released subsequent to the quarter end. The unprecedented action by governments worldwide has limited the volatility in the financial sector considerably. Despite these actions, the illiquidity and concerns of credit markets continues. Financial institutions remain cautious in the finance of debt. As a consequence, many blue chip companies have suffered substantial losses as they struggle to refinance debt.

Global equity markets continued to reflect uncertainty and volatility. The S&P 500 index experienced its worst year since 1931 with a fall of 38% and other bourses across the world have also experienced substantial drops in value (the ASX200 index fell 41%, the Futsi 100 fell 31%). Locally the ASX has experienced a marked slowdown in capital raisings with 24% less capital raised in 2008 than 2007, and a 70% drop in the number of IPO's.

Towards the second half of the quarter commodity prices have begun to stabilise as global panic subsided and price induced cutbacks and mine closures have reduced the scale of forecast supply surpluses. Many analysts are expecting precious metals and a slowly recovering steel demand to lead commodity prices higher in the shorter term. In fact many commodities are close to supply/demand equilibrium with uranium reportedly currently in deficit and showing signs of a price revival and recent improvements in the iron ore spot market in recent weeks.

Over the quarter, the Fund's NTA fell by $0.44 from $1.15 in September 2008 to $0.71 in December 2008 and mirrors the fall in the Small Resources Accumulation Index over the same period. Although it is disheartening that the discount to the NTA has increased from 39% in the previous quarter to 51% in the current quarter, we remain positive that this discount will narrow over time when more rational sense returns to the market. The Fund is of the firm belief that it is well placed into the coming year to capitalise on the various attractive opportunities that the global equity markets have created amongst the world financial turmoil. In essence, asset values are at unprecedented lows and with commodity prices likely to rise over the shorter term, the Fund plans to capitalise on the significant opportunities in the resources sector.

One of the Fund's strategic longer term holdings, Atlas Iron, which commenced mining its Pilbara project only in October 2008, made the successful transition to production with its maiden shipment made on 5 December 2008. Atlas Iron was able to successfully secure off-take arrangements despite the difficult market conditions during this period. Atlas Iron also had a series of promising exploration successes at Wodgina and Abydos during the quarter to complete a standout year for the company. During the quarter the Fund exercised a number of free unlisted call options in Atlas Iron, which were significantly in the money, at a strike price of $0.30. The stock traded at $0.855 on 31 December and has been trading above $1.20 post reporting period.

A disappointing event during the quarter saw both Matrix Metals and CopperCo enter into administration and receivership during the month of November 2008 due to the global credit crunch. Despite strong underlying assets in both these companies and hedging designed to cover operating costs, CopperCo incurred a provisional pricing debt to Glencore who was under contract to purchase copper cathode - resulting in its inability to finance its working capital requirements in the short term. Likewise, Matrix Metals was also unable to finance its operating capital requirements due to pricing debt to Glencore. The Fund however, had written down its equity investment in these companies substantially at the time of receivership but remains well placed to recover the $5m convertible note in CopperCo as this investment is well structured, secured and there is reportedly widespread interest by a large number of parties in CopperCo's assets.

Riversdale Mining is progressing with its feasibility study for the development of the Benga Project in Mozambique, an open cut development of the 2.1 billion tonne JORC resource of coking and thermal coal. The Fund had fortunately sold down a large portion of its holding in Riversdale prior to the past quarter and acquired incremental shares in the company at substantially lower prices in the December 2008 quarter.

Your manager took advantage of market weakness and increased the Fund's investment in West Australian nickel producer Western Areas NL. Western Areas has recently discovered the world's highest grade nickel deposit at Spotted Quoll and has been mining the nearby high grade Flying Fox nickel mine at exceptionally low cash costs of close to US$2/lb.

Post the quarter ending 31 December 2008, the Fund also invested into an emerging ASX listed coal producer through a high yielding secured debt instrument with an enhanced return from a coal production royalty stream and free attached equity options.

Your manager has an excellent track record of operating in past difficult and volatile markets. The management team's experience of operating in debt and equity markets in both bear and bull market conditions also places the Fund in a strong position to take advantage of the many valuable opportunities that may arise. These types of investments will assist the Fund in reducing volatility, lowering downside risk whilst maintaining equity upside and enhancing distribution revenues from the coupons received. Furthermore, the Fund believes the active steps taken throughout the quarter combined with its increased cash holding, credit lines and deal focused investment team will allow it to capitalise on opportunities that will arise throughout the coming year.

# Market commentary

| Commodity | USD price at 30 September 2008 | USD price at 31 December 2008 | Percentage change |
|---|---|---|---|
| Spot Gold | $884.50 | $865.00 | -2% |
| Oil (WTI) | $99.58 | $44.60 | -55% |
| Nickel (Tonne) | $15,600.00 | $10,810.00 | -31% |
| Copper (Tonne) | $6,388.00 | $2,902.00 | -55% |
| Zinc (Tonne) | $1,653.50 | $1,120.50 | -32% |

Gold has been the standout commodity of the quarter with the commodity decreasing slightly in US$ terms but appreciating by 10% in Australian Dollar terms. Gold has become increasingly attractive to investors as they search for sustained value in this uncertain economic period. Demand has been such that there is anecdotal evidence of shortages of physical gold emerging. However, declining oil prices reducing the inflationary outlook and the possibility of a weaker US$ could put pressure on the A$ gold price over the medium term.

Oil has seen the most dramatic slowdown of commodities and subsequent to the quarter end has deteriorated further. Increasingly, delays, cutbacks and cancellations of projects are being announced throughout the industry, together with other responsive measures, as crude prices drop from one investment breakeven level to the next and the realisation dawns that this is no overnight phenomenon. Moreover, this trend has been reinforced by the present severe restrictions on credit and the gloomy world economic outlook. The slowdown in the US economy which remains the world's largest consumer of oil as well as the downward trend of the global economy has triggered fears of a demand shortage in the market, leading to rapid drops in the price of oil and production cutbacks by OPEC.

Nickel has performed poorly over the quarter with the commodity falling a further 31%. The fall in nickel prices stems from heavy declines in stainless steel production (nickel's main end use). However, recent supply cuts from the likes of Xstrata, Norilsk and BHP (post December 2008 quarter) as well as the collapse of pig-iron production should ensure that nickel prices remain at the US$5/lb level for the first half of 2009.

At the onset of 2008, copper was riding high on the back of sustained high prices and the unabated Chinese growth story. However as the fallout from the global financial markets spread, the red metal started to lose much of its shine in the second half of the year creating difficulty for many junior copper players in Australia.

Zinc has fallen 32% over the quarter as its demand for end use products such as construction and transport continue to fall. The quarter has seen job losses at many zinc mines such as Xstrata's McArthur River Mine and OZ Minerals Century Mine and heavy production cuts of 13% for the sector. Furthermore, analysts estimated during the quarter that up to 40% of the Chinese zinc mines were operating at a loss. We anticipate that despite these production cuts, zinc is unlikely to stage a major recovery due to demand decreasing at a far greater rate than the supply of the commodity.

The metallurgical coal market has been similarly affected by the drop off in global steel demand leading to drop in the contract and spot price of metallurgical coal. Prices are expected to fall from circa US $300/t FOB for hard coking coal to circa $US 110/t FOB , whilst this does appear to be a dramatic price drop it remains above the 2007 contract prices and well above the marginal costs for most producers.

Thermal coal remains the cheapest and most prolific form of power generation and demand will not disappear. Whilst international contract prices have fallen from a high of US$190/t to below $100/t, Chinese domestic prices are significantly higher and most analysts forecast a slight increase in thermal coal prices for 2009.

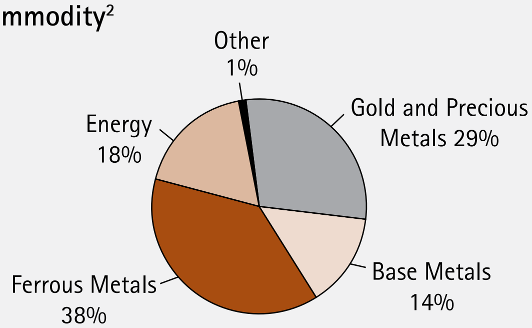
Iron ore has had a tumultuous time of late with the drop in steel demand resulting in companies such as Mt Gibson Iron announcing that its off take customer had requested it put its iron ore shipments on hold. Early on in the quarter the spot market had virtually dried up, however recent signs are that demand from India and China for iron ore is starting to pick up with improved spot prices. As a consequence, Atlas Iron recently agreed off take terms with a medium sized Chinese steel producer and sold two shipments of ore on the spot market. Production cuts by Vale and Rio in the order of 10-15% will assist in supporting 2009 iron ore prices.

The uranium spot price dropped to as low as $45/lb in October – its lowest level since June 2006. However, the spot uranium price experienced upward pressure as utilities and other buyers returned to the market and physical supply returned to deficit with the spot price hovering around $53/lb through to the end of December.

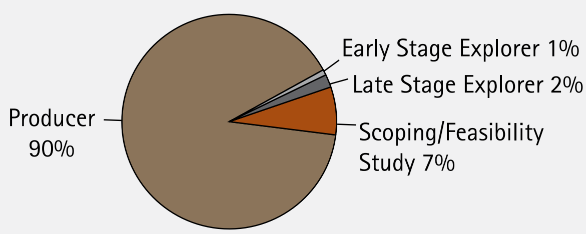
## Linq Resources Fund key market statistics as at 31 December 2008

| | |
|---|---|
| Unit Price (LRF) 30 September 2008 | $0.700 |
| Unit Price (LRF) 31 December 2008 | $0.345 |
| NTA at 30 September 2008 | $1.15 |
| NTA at 31 December 2008 | $0.71 |
| Discount to NTA | 51% |
| Units on Issue[1] | 164.4m |

### Commodity[2]




### Stage of Project




[1] Excludes LRF 2 units which are excluded on a consolidated basis.
[2] Compositions are calculated excluding the amount of cash held by the Fund at 31 December 2008.

# Linq Resources Fund top 5 investments as at 31 December 2008

| Company | Key Project Domicile | Commodity Focus |
|---|---|---|
| Ferrous Resources Ltd | Brazil | Iron Ore |
| Lihir Gold Ltd | PNG, Australia, Ivory Coast | Gold |
| Riversdale Mining Ltd | Southern Africa | Coal |
| Atlas Iron Ltd | Australia | Iron Ore |
| China Gold Mines PLC | China | Gold |

### Ferrous Resources Limited

Ferrous Resources is a large unlisted Brazilian iron ore company. Ferrous has a number of projects located within the world class Iron Quadrilateral region in Brazil. These projects have a current JORC resource of over 2 billion tonnes and over 2 billion tonnes in exploration potential.

### Lihir Gold Limited

Lihir Gold is an Australian listed gold producer in the S&P/ASX 50. Lihir has operations primarily in Papua New Guinea, Australia and the Ivory Coast. The Fund acquired units in Lihir following a merger by scheme of arrangement with one of the Fund's long term investments, Equigold. For the third quarter, Lihir announced record production of 250,000 ounces at low cash costs of $412/oz. The million ounce upgrade of the Lihir Island Mine continues to run on budget and on schedule. The former Equigold Mine, Bonikro poured its first gold over the quarter and is now running at nameplate capacity of 2.4mtpa.

### Riversdale Mining Limited

Riversdale is an anthracite coal producer in South Africa with a large coking coal project in Mozambique. The company's large land holding in Mozambique in the Moatize Basin has been identified as a potential world class coking coal deposit. Within a small area of the Company's total tenement areas (2%), the company has identified a 2.1Bn tonne JORC inferred resource. Initial test work confirms that the Benga Deposit in Mozambique will produce a premium coking and thermal coal product. The South African, Zululand Anthracite Colliery continues to produce circa 850kt ROM coal per year.

### Atlas Iron Limited

Atlas is an iron ore producer in the Pilbara region of Western Australia. During the quarter Atlas commenced production from its Pardoo project and sold its first two shipments of iron ore and secured partial off take to medium sized Chinese Steel Mills. Atlas is aiming to produce 1mtpa during the first 12 months ramping up to 6mtpa in 2010 and 12mtpa in 2012. Atlas continues to produce solid exploration results with new discoveries at Wodgina and Abydos and continuing solid results from the Pardoo project.

### China Gold Mines Plc

China Gold mines PLC is an AIM listed gold producer. In early 2008, China Goldmines poured its first gold to mark the opening of its new production plant at its Shenjiaya Project in China's Hunan province. The project has a global gold resource of 1.83MozAu. Target production for 2009 is 20,000 – 25,000oz Au. The current resource is expected to convert to reserves systematically as development continues and the ore bodies are exposed.. The resources are still open at depth and along 9.5km of strike.

# About the LinQ Resources Fund

The LinQ Resources Fund is a registered managed investment scheme, which successfully completed an initial public offer and listed on the Australian Stock Exchange on 20 January 2005 (ASX code LRF). The Fund's net asset value at 31 December 2008 was $115.1m (unaudited). LinQ Capital Limited is the Responsible Entity of the Fund. LinQ Resources Fund is an actively-managed resources fund which specialises in investments in resources companies both in Australia and overseas.

Further information about the LinQ Resources Fund can be found on the website www.linqresources.com or by contacting info@linqresources.com