February 14, 2012

Australian Enhanced Income Fund
January 2012 Investment Update and NAV

January 2012 NAV

The Fund's NAV at the close of business on January 31, 2012 was $**6.401** per unit. This compares with the ex-distribution NAV of a unit at the close of business on December 31, 2011 of **$6.343**. The change in NAV over the month of January 2012 represents a return of +0.91%. The franking benefit was estimated to be 0.01%**.**

Trading details

The Fund traded at a discount to the most recently published NAV of a unit over the month of January. The volume weighted average price (VWAP) for January 2012 was **$6.18**.

	January 2011
Australian Enhanced Income Fund	+0.91%
UBS Warburg Bank Bill Index	+0.40%

*Returns do not include the benefit of franking. Past performance is not necessarily a guide to future performance.

Events of January

- The ASX listed hybrid sector returned +0.21% for the month. This compares with the All Ordinaries Accumulation Index return of +5.23%,
- The bank hybrid sector underperformed as the issuance of covered bonds pushed spreads on bank hybrid debt wider.

Fund and security performance

The Fund outperformed the broader market this month on the strength of the Fund's underweight position in bank hybrids which under performed. Positive return contributions came from TPAPA (+9.3%) and GMPPA (+5.5%) while WCTPA (-2.6%) and ANZPC (-1.2%) detracted from performance. The Fund's net return (excluding franking) for the year ended January 31, 2012 was 0.77% from 0.82% previously.

Covered bonds and the impact on traded margins

As we've mentioned in previous reviews the European banking system is dysfunctional. This is not good news for the Australian banks as they not only face chunky borrowing targets this year of around $90b but they are heavily reliant on European sourced term funding. To offset their reliance on European sourced term funding and to help replace the maturing government guaranteed debt issued in 2009 and 2010 the banks were permitted to issue so called "covered bonds" late last year. However, the recent capital market freeze in Europe pushed the net cost (after swaps) of issuing covered bonds into Europe to around 2.25% or about 1% higher than the banks had originally thought. Eventually the banks decided to issue covered bonds to Australian institutions at a margin of around 1.7%. In view of the 'seniority' of covered bonds this helped propel the margins on domestic bank bonds, including listed hybrid debt wider by about 30 basis points.

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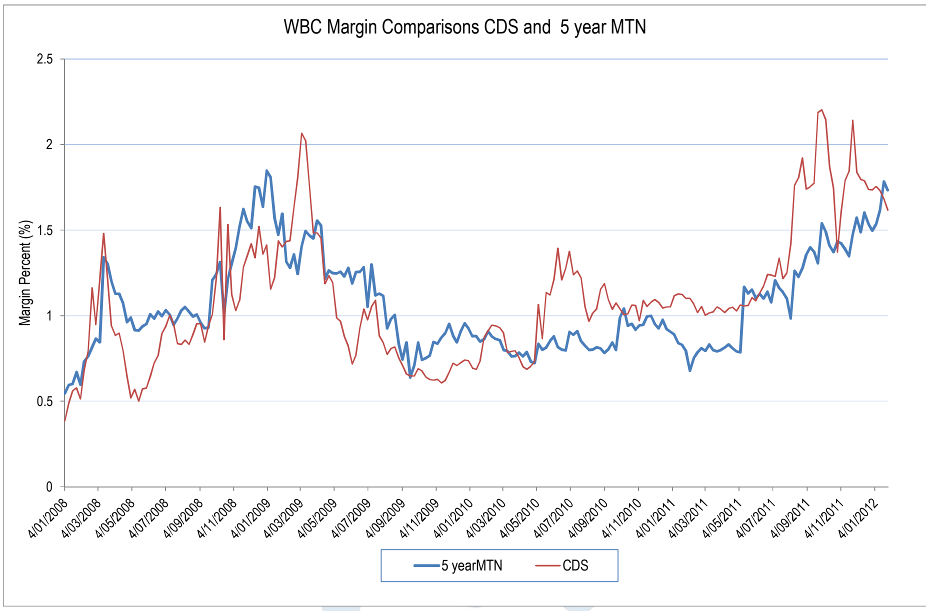
Bank margins: we're back to 2008

The chart below shows the margins on a 5 year WBC bond and the WBC credit default swap (CDS). Although not a perfect match both indicate that margins are now approaching GFC levels. While time desensitizes things what is happening now in Europe doesn't feel anything like a GFC type event. In support of this the global equity markets have ceased falling and volatility has declined.



Issued capital and NAV as at close of business 31 January 2012

	31 January 2012	Previous month	Monthly change	Change over Quarter
Total number of ordinary units	3,047,223	3,043,166	+4,057	(36,108)
Net Asset Value (NAV)	$6.401	$6.343*	+0.91%	+0.20%

* Ex Distribution. Returns exclude the franking benefit. Past performance is not necessarily a guide to future performance.

Performance History

	Sept 2011	Oct 2011	Nov 2011	Dec 2011	Jan 2012
Change in NAV	-0.48%	+3.94%	-1.67%	+0.98%	+0.91%
Change in UBS Bank Bill Index	+0.39%	+0.42%	+0.39%	+0.39%	+0.40%
Comparison to Bank Bill Index	-0.89%	+3.52%	-2.06%	+0.59%	+0.51%
Franking benefit (*estimated*)	+0.12%	+0.06%	+0.10%	+0.08%	+0.01%
Total Return including franking	-0.36%	+4.00%	-1.57%	+1.06%	+0.92%

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