MAGELLAN FLAGSHIP FUND LIMITED

2009 ANNUAL REPORT

CONTENTS

CHAIRMAN'S LETTER

Dear Shareholder,

I am pleased to write to you in the 2008/9 Annual Report for Magellan Flagship Fund Limited ("MFF") and encourage you to take the time to read the financial accounts and the Investment Manager's Report which follow.

FINANCIAL RESULTS

Although MFF's portfolio outperformed the major equity market indices, you will see that MFF recorded a loss after tax for the year of $14.7 million (or 3.96 cents per share). This reflects the 'mark to market' of all market price movements for the year. Market based measures are volatile and year to date figures show a profit from 'mark to market' price movements. Overall, the movements in foreign exchange in the year benefitted the Company by about 10 cents per share whilst the fall in market prices of the portfolio in base currencies was approximately 15 cents per share.

The decline in MFF's pre tax net tangible assets of 5 cents per share (7.4%) for 2008/9 compares with declines of approximately 31% for the major global indices (or approximately 18% in AUD adjusted terms) and approximately 24% for the major Australian index. Whilst your Directors are not pleased to report a decline, we consider that MFF handled the extreme conditions of 2008/9 better than many. We are also confident about the business prospects for the high quality companies in the MFF portfolio. We expect that MFF's focused, disciplined investment approach will be rewarded with sustained positive performance, over time.

As all investors are aware, equity markets in 2008/9 were very difficult and volatility also continued in currency markets. We encourage you to read the Reports and accounts and we expect that you will see why your Directors have grounds to be pleased with many aspects of the investment performance in 2008/9 and why we have confidence, notwithstanding the ongoing global economic turmoil.

MFF'S PORTFOLIO

During 2008/9 market prices fell week after week for many companies, even including the market prices of the strongest companies. Many major companies and overall indices traded at levels below those prevailing a decade ago.

In this environment, the MFF portfolio was further upgraded with purchases of select companies with global leading businesses. More significant portfolio acquisitions included shares in Nestlé, Yum! Brands, Wal-Mart, Google, Coca-Cola, Procter & Gamble, McDonald's, Tesco, Colgate-Palmolive, Visa and MasterCard. Each of these companies is a global leader in its field, generates very substantial cash flows and earns returns on invested capital that are well in excess of its cost of capital.

MFF also progressed its on-market buy-back and moved towards a fully invested position by financial year end. We expect that MFF shareholders will benefit over time from these decisions.

MFF's portfolio is more than 95% invested in leading global multinationals. The top 20 holdings are detailed in the Reports. Almost all of these companies have leadership positions (with both suppliers and customers) in emerging markets as well as in the (currently recessed) more developed markets. In the current difficult ongoing economic conditions, we expect the earnings of our investee companies to continue to demonstrate well above average resilience, although no company is recession immune. It is also highly probable that these companies have satisfactory upside potential from future economic recovery and income growth.

Whilst MFF's portfolio companies are not insulated from the chill winds of the recession despite excellent business resilience, they will likely be disproportionate beneficiaries of the 1 billion or so newly middle class, newly urbanised consumers expected over coming decades in emerging markets.

Importantly, the investment manager regards the market prices for MFF's investment securities as being inexpensive relative to their demonstrated earnings power. As discussed in the Investment Manager's Report, investors' caution, pessimism and panic translates into far lower equity prices than when investors are ebullient.

Your Directors continue to be satisfied with the Investment Manager's selection of MFF's high quality portfolio and its disciplined focus upon seeking superior risk adjusted returns on a rolling 3-5 year basis. We note the outperformance versus indices, although we all want positive returns.

MFF continues to provide valuable diversification for Australian and New Zealand investors in terms of companies, currencies and business geographies. We are pleased that MFF maintained its investment discipline and, particularly, that MFF continued to buy shares in quality businesses during the panic and widespread falling prices in 2008/9. The Investment Manager's Report includes commentary around currencies as well as MFF's investments.

ON-MARKET SHARE BUY-BACK

In July, 2009 MFF completed its on-market share buy-back of 20 million shares at an average price of approximately 56 cents per share, which represents a discount to MFF's net assets per share. MFF today announced that it will undertake a further on-market share buy-back of up to an additional 20 million MFF shares over the next 12 months. Shares bought back will subsequently be cancelled. MFF's Balance Sheet is strong, with its investments in highly liquid shares and a modest level of borrowings in comparison with investment assets. We intend to maintain MFF's Balance Sheet strength after shares are bought back.

ANNUAL GENERAL MEETING

My fellow Directors and I look forward to meeting those of you who can attend the Annual General Meeting at 11.00 am on Tuesday, 20 October, 2009 in the Investor Presentation Room at Magellan's offices:

Level 7, 1 Castlereagh Street
Sydney NSW 2000

Yours faithfully,

Richard F E Warburton AO
Chairman
26 August 2009

INVESTMENT MANAGER'S REPORT

Dear Shareholder,

INTRODUCTION

In this Report we update you on MFF's investment portfolio, which was strengthened further in 2008/9. My key partner, Hamish Douglass, and I are delighted with the quality of the companies in the MFF portfolio. As shareholders in MFF, you (and we) own some of the most outstanding businesses in the world. We also have no doubt that their aggregate competitive advantages increased in 2008/9 as they responded to the global recession. However, the financial crisis damaged the balance sheets and prospects of businesses, Governments and individuals worldwide, and full restoration of confidence (and business values) is not automatic despite recent market rallies and some optimistic indicators.

The pain and pessimism in financial year 2008/9 presented some mouth watering purchase opportunities and MFF sought to target its finite resources upon those that offered the best risk adjusted opportunities. In the very stressed business environment, panicked and forced sellers were desperate to unload shares at low prices, as did momentum followers and short sellers. Although many prices have recovered somewhat, we remain very positive about our portfolio's attractive prices having regard to expected future earnings power, prevailing and prospective interest rates and other investment opportunities that we review.

In the 2 ½ years since MFF commenced, debt and equity markets capitulated, world economies deteriorated and markets capitulated again. The future remains uncertain, as always, and confidence is a crucial variable particularly given global interconnectedness. We are very confident that our investee companies will sell more goods and services around the world over the next 5 to 10 years, and investors will value these outstanding businesses at a premium, in time. We expect an eventual "premium for quality" when our companies' cashflow generation is rewarded positively, whether or not the economic recovery is rapid.

We are optimistic for future growth in global living standards, particularly in emerging markets, notwithstanding the numerous challenges around the world. Analysts and economists are divided on whether inflation or deflation will predominate in 2010 and coming years. We have invested in businesses that have the pricing power and other competitive advantages in order to prevail in either inflationary or deflationary environments. We intend to hold onto our collection of businesses which combine extraordinary free cashflow generation, above average global growth prospects and sustainable competitive advantages.

Despite our optimism, there remains very significant economic challenges and further periodic market corrections are inevitable. Some bubbles have already re-emerged and we do not seek to predict their extent or duration. We underestimated the recovery in Australia's GDP and terms of trade (as the Reserve Bank said recently, Australia's export recovery has been 'remarkable') and hence we missed out on generating relatively 'easy' profits for MFF by not implementing a partial hedge of our non-AUD exposure in early 2009. We expect future currency volatility, and a continuation of the upward momentum of the AUD would continue to hurt results. Record speculative flows into commodity funds and 'carry trades' support the currency's upward move, whereas the very weak underlying demand from consumers has been a lesser countervailing influence in 2009.

PORTFOLIO UPDATE

MFF's outperformance relative to various Australian and international indices is mentioned in the Chairman's letter. MFF's market values declined in the financial year, with the rapid rise in the AUD in the fourth quarter being an obvious drag. The quality of the portfolio and the relatively attractive valuation of its components gives us confidence that we will reverse this decline in coming years. A number of our investments trade at prices below those of a decade or more ago despite at least doubling their ongoing earnings and cashflows.

MFF's Top 20 holdings at market value as at 30 June 2009 comprised 97.47% of MFF's portfolio and are shown below:

	$Am Market value	% of Portfolio		$Am Market value	% of Portfolio
American Express	39.9	14.39%	Tesco	9.0	3.26%
Nestlé SA	34.4	12.40%	Colgate-Palmolive	7.1	2.57%
Yum! Brands	34.0	12.28%	Unilever NV	6.5	2.34%
Wal-Mart Stores	28.7	10.36%	Bank of America	6.1	2.19%
eBay	21.3	7.67%	Lowe's Co Inc	4.5	1.62%
PepsiCo	18.3	6.59%	Johnson & Johnson	4.0	1.45%
Google	13.1	4.72%	Visa	3.9	1.41%
Coca-Cola	12.8	4.60%	Cintra	2.0	0.72%
Proctoer & Gamble	11.4	4.13%	Mastercard	1.7	0.61%
McDonald's	9.9	3.58%	US Bancorp	1.7	0.60%

We maintained or increased share holdings in American Express, Nestlé, Yum! Brands, Wal-Mart, eBay, PepsiCo, Google*, Coca-Cola, Procter & Gamble, McDonald's*, Tesco, Colgate Palmolive*, Visa* and MasterCard* during the financial year (*signifies new to the Top 20 in 2008/9).

We hold the only 2 Dow Jones Industrials components to rise in the carnage of calendar 2008 (Wal-Mart and McDonald's), and the best performer to date in calendar 2009 (American Express). Note that we do not aim to chase short-term results.

The portfolio is concentrated in the global leader (or #2) in categories that are very profitable (and will likely continue to be, for decades) and where it is highly probable that our companies will maintain their industry leadership. Whilst our portfolio is being impacted by the global recession, the resilience in earnings and business strengths is far above average. This portfolio is also concentrated in companies which already have profitable leadership in the largest emerging markets and, we believe, meaningfully above average future growth prospects. Hence many of these businesses may be seen as combining attributes of defensive and growth companies. Their reaction to the global recession demonstrates how these companies have multiple levers in times of adversity, and how well they are using technology and productivity gains to help profit margins.

MFF was focussed resolutely on quality and value in 2008/9, as we sought to take advantage of the best prices for buyers of securities in quality companies for more than 20 years. We also sought to avoid numerous land mines, and analysed and re-analysed the business strengths and weaknesses of our investee companies under the most stressed economic scenarios. In order to fund this buying, and MFF's share buy-back, we utilised nearly all of MFF's available resources and sold some investments where business risks appeared to be rising unacceptably, where prices approximated our assessment of fair value (which happened very briefly in 2008/9) or where we assessed better risk adjusted opportunities.

INVESTMENT DISCUSSION

Our primary investment goal is to increase the per-share asset backing of MFF. We focus first on seeking to create intrinsic value (which in 2008/9 was very different to market price as 'Price is what you pay. Value is what you get'). However, in time, market prices for quality companies revert towards intrinsic value. Thus, if our purchases were at prices below sustainable intrinsic values, we expect that this will be reflected in increased book value per share. If this occurs, it will also be reflected in an improved price for MFF shares.

Our investment approach remains clear:

We want to buy, at discounted prices, shares in companies that we feel we can understand, that have strong business positions that generate high returns on invested capital and high levels of free cashflow and where, ideally, the probability is that those strong market positions will continue to improve over time. Hence, positive future returns should be more predictable and resilient than for most businesses. Note that business risk and cycles are not eliminated in this approach, as shown by the impact of the crisis upon even the best capitalised financials. In our ideal businesses, high future returns on invested capital and free cashflows are highly likely,

INVESTMENT MANAGER'S REPORT (CONTINUED)

as these businesses strengthen their leading market positions around the world.

The global recession has highlighted the huge levels of overcapacity in most industries and accelerated some secular technological changes (walk through a mall in Europe or North America or compare online and traditional media to demonstrate). The implications of these types of issues are wide ranging but hard to predict, as are short-term moves in markets or economies (for example, what will be the impact of the inevitable restocking of inventory that has been rundown and what allowance should be made for the runoff of current Government stimulus in considering future economic figures). We feel that by narrowing our focus and by lengthening the duration, we increase the probability of making a better assessment of the sustainability of businesses' competitive advantages.

Although we invest on an individual business by business basis (and, for example, seek the lowest cost players in an industry), you may seek to categorise some of our investee companies according to the following longer-term sustainable investment trends:

- We believe that a small number of multi-decade 'global winners' are selecting themselves amongst fast moving consumer goods (FMCG) companies. These companies are the global leaders in their categories and have product, innovation, marketing, brand and distribution strengths and are growing rapidly in emerging markets as incomes rise [examples include Nestlé, Yum! Brands, PepsiCo, Unilever, Procter & Gamble, L'Oreal*, Coca-Cola, McDonald's, Colgate-Palmolive and the consumer division of Johnson & Johnson]. Demographics are favourable for the foreseeable future as more than a billion people are moving from poverty to more middle class living standards and there is a related move of more than a billion people to urban dwelling.

- We believe that a very small number of the leading, strongly capitalised, retail focused banking and financial institutions will emerge after the current financial crisis with enhanced market shares, profitability and low funding costs [examples include American Express, Visa, MasterCard, Bank of America, US Bancorp and Wells Fargo].

- We believe that the lowest cost, market leading, non-discretionary retailers offer excellent customer value and satisfaction propositions in recessionary as well as recovery scenarios (for example Wal-Mart, Tesco, Lowes and Home Depot* have significant non-discretionary merchandise alongside more discretionary offers).

- We are attracted to the best global 'networks' and these may strengthen further over coming decades (American Express, eBay and Google are examples). Our FMCG companies, financials and retailers also have network economic benefits as do our investments in healthcare (Johnson & Johnson, Stryker) and technology systems (Microsoft, IBM).

(indicates holdings sold in 2008/9)*

Even in the recent partial market recovery, the prices of many of these companies has remained attractive. The most attractive prices tend to occur where investors are concerned about the near-term prospects for a quality business, either in comparison with other prospects or in absolute terms. Two recent examples of attractive relative valuations because the crowd has been focussed elsewhere are McDonald's and Wal-Mart, which are regarded by many as being defensive despite very significant ongoing increases in customer numbers.

We have an optimistic underlying philosophy. We believe that people are resilient and aim to improve their living standards. We also believe that technological and other productivity benefits will continue. There are fewer wars globally than in past decades (although this can change rapidly) and the reaction to the crisis by most countries around the world, including emerging Asia and Europe, has been to recommit to economic progress despite the pain. The European Union has been a significant economic success, including via lowering overall borrowing costs, despite bureaucracy, periodic tensions and ongoing strains.

During 2008/9 our resolve was tested. Prices declined from levels we regarded as already very low. A vicious negative feedback loop was in operation. Debt markets seized up as major financial institutions were threatened or collapsed, and this fear dragged otherwise sound institutions into the vortex. Falling share prices caused fear and panic in markets and translated into collapsing business and consumer confidence, which slashed near-term business prospects and caused further fear and panic in markets as the worsened prospects 'justified' further lower asset prices and risk aversion. There was real risk of an even broader collapse of the financial system and this added to the fear and panic. This fear and panic manifested itself in many ways, including negative short-term US Treasury prices (in other words, scared investors were willing to pay money to receive a lower face value in 3-6 months for US Treasuries, rather than 'risk' investing their money in other assets).

Central banks and governments injected unprecedented stimulus and appear to have finally stabilised the markets. Companies are now dealing with the recession, consequences of the financial crisis and with the implications of the stimulus itself. The Chairman of Nestlé has often used the metaphor that "it is the descent from the summit that is most dangerous" and we believe that unwinding the unprecedented stimulus will not be incident free.

In this context, we sought to detach ourselves from the incessant 'noise' of the market. We focussed upon the underlying businesses and sought to test and retest our assessments of business cases. In the year we bought shares in outstanding companies at prices that we simply did not expect. As MFF does not have cash inflows from other businesses or from new inflows, like an equity mutual fund, we used some resources we had held aside and sold weaker business cases and situations where prices were closest to our assessment of fair value. Some previous investment mistakes were also plainly exposed. We reallocated, rather than withdraw to cash, given our strong views on favourable valuations (rather than any insight into short-term market movements).

The crisis required detailed re-evaluation of business strengths. Sustainable competitive advantages can be illustrated as follows. On average, each day this year the Coca-Cola system is likely to sell about 1.6 billion non alcoholic drinks (despite the crisis). Coca-Cola earns a net profit after tax of less than 1½ cents on each drink, and convenience stores and other retailers are anxious to stock these products as they earn good margins on their high velocity sales to consumers. The combination of favourable products, global distribution, affordable prices and focus have combined to cause Coke's volumes and competitive advantages to continue to rise for decades, as happened this year with markets such as China growing in double digits. Similarly, investors simply have to observe Wal-Mart's supercentres to see that a virtuous circle of lower prices and better range is operating to increase Wal-Mart's competitive advantages in comparison with other mainstream retailers. Shares in these 'almost inevitable' ongoing business success stories have traded this year at lower metrics than companies here and elsewhere with far less advantaged businesses or prospects.

MFF's largest current holding, American Express, was positively rated in the US Treasury 'stress test' review of 19 large financial organisations in early 2009. Their credit metrics have improved and management reacted well to protect the business through the crisis. We believe that, in time, American Express will again be valued by investors based upon its strong earnings power and ongoing growth, although the recession caused meaningful credit losses and card member spending has declined. We added to the position in 2008/9 (modestly given the existing weighting), including a small purchase below $10 per share on March 6, when the market panic was at its highest level.

CAPITAL MANAGEMENT

MFF completed a 20 million share buy-back in July 2009 at an average price of approximately 56 cents per share. Directors have authorised a new on-market buy-back up to a further 20 million shares. Whilst we recognise that there are arguments on either side of the debate, the ongoing market and economic uncertainty indicates that there are reasonable prospects for MFF to buy back shares on terms that are value accretive for shareholders, as we believe was the case in 2008/9. We also did not follow the current fashion of issuing new shares, as we believe this is dilutive for many existing shareholders and not in your interests, even though a cash injection at the bottom of the market would have worked wonders for the manager's investment performance statistics!

MFF's gearing has risen closer to our 20% limit after completion of the initial buy-back and purchases in recent months of selected high quality companies such as Coca-Cola, Wal-Mart and McDonald's, as the rally progressed elsewhere. We will adhere to the gearing limit as the ongoing buy-back progresses. MFF currently benefits from the unsustainably low interest rates; these are well below our portfolio companies' free cashflow yields in most cases and below dividend yields in some cases. Many of our companies have the competitive advantage of generating billions of dollars of stable free cashflow each year, and some, such as Nestlé, used their financial strength to undertake borrowings during this crisis year at rates below LIBOR (the inter bank rate).

INVESTMENT MANAGER'S REPORT (CONTINUED)

OTHER COMMENTS

Overcapacity is prevalent around the world, for example in retailing in developed markets, in most manufacturing industries and in labour supply. Whilst some of this is cyclical because of the downturn, much is structural. Some is a by product of globalisation that shifts manufacturing and other activities to less expensive locations. Economic performance country by country will be differentiated by ongoing small business formation, which utilises new technology and often requires re-skilling, access to funding (home equity loans in the past) and reduced Government red tape (or even partnership/co-operation with Government).

When the immediate benefits of fiscal and monetary stimulus dissipate, surplus capacity will likely continue to diminish investment returns and pressure prices for many products and services, unless aggregate consumer demand rebounds strongly. Whilst we expect some positive GDP 'surprises' in 2009 and 2010, this is very different to widespread sustainable multi-year profitable growth. Increased tax burdens to repay Government stimulus and/or higher inflation lie ahead. The real purchasing power of unskilled labour in developed economies has fallen, or at least not grown, in comparison with returns to skilled labour and to capital over the past decade. As access to consumer credit tightens, this trend has obvious implications for aggregate consumption and its mix.

We seek to assess and reassess market dynamics for companies and industries in which we are interested. Do a small number of industry participants generally have pricing power? Why? Who has the lowest input and distribution costs? How reliant are they upon customers/ suppliers/ governments/ distributors/ employees that may curtail returns? What is the foreseeable current and future impact of technology changes? Objective answers to these types of questions are important in assessing whether companies might have sustainable competitive advantages. We seek to be objective and our focus on value means we prefer to buy companies that are out of favour or at least 'boring' to many others.

We attempt to increase our understanding of important markets, such as oil supply and demand. Global petroleum usage has declined in the recession from about 88 million barrels per day to about 85 million. The US motorist is currently a key factor in terms of demand, with the US consuming about 25% of daily oil usage and about 55% of that is used to power the 200 million + consumer motor vehicles. As the marginal cost of production of oil is well below the market price, producers have not meaningfully rationed supply over past decades and probably will not in the future. Hence, the world is vulnerable to Peak Oil if left simply to the working of market forces. Market forces may result in a rapid crossover from relatively plentiful, relatively inexpensive oil to shortages and price shocks.

Thus, we are looking at US Energy Policy as it evolves. Similarly the recent rapid improvement in commercialisation of hybrid and other long life battery motor vehicles is very meaningful. As well as impacting oil usage downward, foreseeable future benefits of improved battery technology also include storage of electricity at solar and wind facilities, and improvements in the cost effectiveness of desalination. Major technological advances and commercialisation will have profound impacts, including on food production as well as on energy cost and usage.

Implications for global fund flows would be significant. At the moment the US imports about 55% of its oil requirements and the US $300bn (approximate) annual cost also approximates its annual trade deficit. China, as an increasing energy importer, will also benefit from meaningful progress in behavioural and technological changes. China is also encouraging its entrepreneurs in chasing battery and other energy technology. Periodic oil and other commodity price volatility and upward spikes will likely occur, even if Government policy and business responses are positive overall and avert a full blown crisis.

Technology is a key to averting the raw material, water and food shortages and price rises that appear inevitable without further advances. Such advances are not guaranteed and outcomes could vary substantially in coming decades. Ongoing technology benefits for business and government (for example, in reducing real inventory, traffic and transport costs), and ongoing advances in consumer technology are also inevitable. Technology has been, and will continue to be, crucial in enabling entrepreneurs and this small business growth had offset a large proportion of the labour oversupply prior to the recession. We seek to do our best to select companies that are likely to be well positioned for these foreseeable technology changes. We remain concerned that the consequences of the economic downturn have a long way to play out.

Corporate pessimism remains widespread with many insolvencies, layoffs and deferral of capital expenditure. However, capital markets have improved, including much stronger debt and equity issuance which is averting many big company balance sheet crises. Many markets have rebounded from very low levels and some have returned to frothy speculation.

We remain very cautious about the near-term economic outlook, the current level of speculative flows and the future effects of the current political reactions to the crisis. Funding of Government Debt is an increasingly important issue, as is the poor health of securitisation markets. Investors and politicians should not 'declare victory' too early as complacency and over confidence carry significant future risks. Consumer deleveraging is occurring, is likely to continue, and is likely to impact underlying GDP and resource demand.

Confidence is a key factor and this includes corporate and consumer confidence. Market participants are watching confidence levels and trying to assess the possible severity and duration of the impact of the recession. This is a difficult task, as confidence fluctuates in response to multiple variables. For example, some economies with the highest level of consumer indebtedness recently have experienced rising confidence levels, as the unprecedented levels of fiscal and monetary stimulus have their initial impacts. Budget deficits matter: for example, the clearing of US housing inventory is slow, partly because the US system of 30 year fixed rate mortgages have rates above 5% p.a. compared with near zero cash rates. The fear of inflation contributes to these elevated rates [mortgage rates in countries which rely more on variable rates are even more impacted by actual inflation].

CURRENCIES AND INFLATION

We discussed currencies and inflation in some detail in previous reports, including in the 2008 Annual Report. The fundamental arguments remain, with a number borne out during the last 12 months. Based on current markets and policy settings, MFF will continue with its unhedged position (subject to the relatively small impact of foreign currency borrowings, as most borrowings currently are in AUD). We continue to aim for currency to be a moderate positive influence on performance over time, and we will promptly advise the ASX if MFF engages in any substantial currency hedging in response to changed market conditions. MFF continues to provide valuable diversification (by geography, company and currency) for Australian and New Zealand investors, many of whom are concentrated in AUD assets.

MARKET UPDATES

Investors can track the portfolio and its underlying price movements, as we report MFF's net tangible asset backing to the ASX on a weekly basis and also advise changes to the portfolio regularly. Please remember that market prices are only one reference point for investors and should not guide them in assessing underlying business performance. As shown by the dramatic moves over the last 12 months, market prices are simply the aggregate weighting of the world of investors, speculators, short sellers, forced sellers, company buying and all other buyers and sellers at a point in time, and are often just a distraction from focussing on business fundamentals. Individual prices can be far above or below fair value at any time. On average and over time, a company's ability to generate free cashflow and deploy it favourably for shareholders is the #1 influence on the direction of its share price. Ideally, in time, we will all look back on the events of 2008 and 2009 as having produced the best opportunities in a generation for investing in quality companies.

We look forward to seeing you at the Annual General Meeting in October. You may also be interested in Hamish's recent commentary in relation to the Magellan Global Fund which includes reviews of Nestlé and of global markets. It is available from Vanessa Hall (02 8114 1859) or on our website: www.magellangroup.com.au.

Yours faithfully,

Chris Mackay

Chris Mackay
Chief Investment Officer
26 August 2009

DIRECTORS' REPORT

The Directors of Magellan Flagship Fund Limited (the "**Company**") submit their report in respect of the year ended 30 June 2009.

DIRECTORS

The following persons were Directors of the Company during the year and up to the date of this report unless otherwise noted.

Name	Directorship	Appointed
Richard Warburton AO	Chairman and Independent Non-Executive Director.	19 October 2006
John Ballard	Independent Non-Executive Director.	19 October 2006
Andy Hogendijk	Independent Non-Executive Director.	19 October 2006
Chris Mackay	Non-Executive Director.	29 September 2006
Hamish Douglass	Non-Executive Director.	29 September 2006

RESULTS AND REVIEW OF OPERATIONS

The Company recorded a net loss for the year after income tax of $14.7 million (2008: $76.3 million loss) principally as a result of the impact of exchange rate movements on foreign currency borrowings and changes in the market value of investments. Overall, the movements in foreign exchange in the year benefitted the Company by about $0.10 per share whilst the fall in market prices of the portfolio in base currencies was approximately $0.15 per share, resulting in a net per tax NTA per share decrease of $0.05 over the year.

The Company's net tangible assets (NTA) per share excluding deferred tax assets at 30 June 2009 was $0.63 (30 June 2008: $0.68). The movement of $0.05 in the NTA per share over the year reflects changes in the market price of investments in their base currencies and changes in the value of the Australian dollar against the foreign currencies in which these investments are quoted, as well as income, such as dividends, and operating expenses.

The Company completed the on-market share buy-back of 20 million shares at a total cost of approximately $11.2 million on 30 July 2009. Further details of the buy-back are provided in notes 8 and 15 to the financial statements.

PRINCIPAL ACTIVITY

The principal activity of the Company during the year was the investment of funds into listed international and Australian companies, perceived by Magellan Asset Management Limited (the "Investment Manager") to have attractive business characteristics, at a discount to their assessed intrinsic value.

SIGNIFICANT CHANGES IN STATE OF AFFAIRS

There were no significant changes in the state of affairs of the Company that occurred during the financial year not otherwise disclosed in this report or the financial statements.

EVENTS SUBSEQUENT TO THE END OF THE FINANCIAL YEAR

On 30 July 2009 the Company purchased 7,573,149 shares for consideration of $4.5 million, completing the on-market buy-back of 20 million shares reducing shares on issue to 358,000,005.

On 26 August 2009 the Directors authorised a further buy-back programme of up to 20 million shares.

Since 30 June 2009, the Directors are not aware of any matter or circumstance not otherwise disclosed in this report or financial statements that has significantly or may significantly affect the operations of the Company, the result of those operations or the state of affairs of the Company in subsequent financial periods.

LIKELY DEVELOPMENTS AND EXPECTED RESULT OF OPERATIONS

The Company will continue to pursue its investment objective which is to increase the net asset value of the Company. Please refer to the Chairman's Letter and the Investment Manager's Report respectively for further information.

The methods of operating the Company are not expected to change in the foreseeable future.

ROUNDING OFF OF AMOUNTS

The Company is of a kind referred to in the Australian Securities and Investments Commission's Class Order 98/0100 (as amended) and consequently amounts in the Directors' Report and financial statements have been rounded off to the nearest thousand dollars in accordance with that Class Order, unless otherwise indicated.

ENVIRONMENTAL REGULATION

The Company is not subject to any particular or significant environmental regulation under either Commonwealth, State or Territory legislation.

AUDITOR

Ernst and Young continues in office in accordance with section 307C of the Corporation Act 2001.

NON-AUDIT SERVICES

Details of the amounts paid or payable to the auditor (Ernst and Young) for audit services provided during the year are set out below. No non-audit services were provided during the year.

	30 June 2009 $	30 June 2008 $
Audit and review of the financial reports	102,000	66,000
Total Services	**102,000**	**66,000**

AUDITOR'S INDEPENDENCE DECLARATION

A copy of the Auditor's Independence Declaration as required under section 307C of the Corporations Act 2001 is set out on page 18.

INFORMATION ON DIRECTORS

Richard Warburton AO
Independent Non-Executive Director and Chairman of the Board

Richard Warburton is one of Australia's most prominent company directors. Prior to becoming a professional director, he was the Chairman and Chief Executive Officer of DuPont Australia and New Zealand where he was responsible for DuPont's petro-chemical business operations in Australia and New Zealand.

Dick is currently Chairman of Tandou Limited (appointed April 2008), The Board of Taxation and a Director of Citigroup Limited. He was previously Chairman of David Jones Limited, AurionGold Limited and Caltex Australia Limited (appointed July 1999, resigned April 2008), and a director of Tabcorp Holdings Limited (July 1999, resigned November 2006), Southcorp Limited, Nufarm Ltd (appointed October 1993, resigned November 2007), and the Reserve Bank of Australia. Dick is a Fellow (and former National President) of the Australian Institute of Company Directors.

DIRECTORS' REPORT (CONTINUED)

John Ballard
Independent Non-Executive Director and member of the Audit and Risk Committee

John Ballard has extensive senior executive experience across a wide range of industries. He was previously Managing Director and Chief Executive Officer of Southcorp Limited; Managing Director, Asia Pacific, for United Biscuits; Managing Director, Snack Foods, for Amatil Limited; a director of Woolworths Limited and Email Limited; Chairman of Wattyl Limited; and a director of CSR Limited and subsequently Rinker Limited.
John is currently a director of Fonterra Co-operative Group Limited (appointed May 2006), a trustee of the Sydney Opera House Trust, and Chairman of the Advisory Funds at Pacific Equity Partners. John is a Fellow of the Australian Institute of Company Directors.

Andy Hogendijk
Independent Non-Executive Director and Chairman of the Audit and Risk Committee

Andy Hogendijk has extensive senior management and finance experience having previously been Chief Financial Officer of Suncorp Metway Limited (1997 - 2000), Commonwealth Bank of Australia Limited (1991 - 1997) and John Fairfax Group (1989 - 1991). He has also held several senior positions with Shell Company Australia and Australian Paper Manufacturers.

Andy is currently a director of AWE Limited (appointed October 2007), and was previously a Chairman of Gloucester Coal (appointed August 2004, resigned June 2009), and a director of Aditya Birla Minerals Limited (appointed March 2006, resigned November 2007), Hills Motorway Management Limited and Magnesium International Limited. Andy is a Fellow of the Australian Society of Certified Practising Accountants and the Australian Institute of Company Directors.

Chris Mackay
Non-Executive Director and member of the Audit and Risk Committee

Chris Mackay is the Chairman and Chief Investment Officer of Magellan Financial Group Limited (appointed November 2006) and a director of Magellan Flagship Fund Limited. Chris has considerable experience in business management, capital allocation, risk management and investment. He became an investment banker in 1988, after being a corporate and banking lawyer, and has broad experience in the financial and corporate sectors over many years. Chris is a director of Consolidated Media Holdings Limited (appointed March 2006), and a former director of New Privateer Holdings Limited (appointed April 2006, resigned August 2007), and Crown Limited (appointed July 2007, resigned March 2008). He retired as Chairman of the investment bank UBS Australasia, in March 2006, having previously been its Chief Executive Officer. He is a member of the Federal Treasurer's Financial Sector Advisory Council, and is a former member of the Business Council of Australia and director of the International Banks and Securities Association.

Hamish Douglass
Non-Executive Director

Hamish Douglass is the Managing Director and Chief Executive Officer of Magellan Financial Group Limited (appointed November 2006) and a director of Magellan Flagship Fund Limited and Magellan Asset Management Limited. Hamish has more than 18 years experience in financial services and was, until recently, Co-Head of Global Banking at Deutsche Bank, Australasia. He has extensive experience in the financial services industry and has advised on some of the largest corporate transactions in Australia. He is a member of the Australian Takeovers Panel and a member of the Forum of Young Global Leaders - World Economic Forum.

David Simpson
Company Secretary

David Simpson is the Company's Consulting Counsel and Company Secretary. David is Consulting Counsel and Company Secretary of the Investment Manager and its parent Magellan Financial Group Limited. David has over 20 years of experience as a corporate lawyer. He was a partner in Freshfields Bruckhaus Deringer ("Freshfields"), one of the world's largest law firms, and before that was a partner in one of Australia's leading law firms, Allen Allen and Hemsley (now Allens Arthur Robinson). From 1991 to 2004, David was based in Asia, in Indonesia and Singapore.

Leo Quintana
Company Secretary

Leo Quintana is the Company's Legal Counsel and Company Secretary. He is also Legal Counsel and Company Secretary of the Investment Manager and its parent Magellan Financial Group Limited. Leo has 8 years of experience as a corporate lawyer. He is admitted as a solicitor of the Supreme Court of New South Wales and previously was an associate - commercial and corporate group, of Harris Friedman Hyde Page Lawyers.

DIRECTORS' MEETINGS

The following table sets out the number of meetings of the Company's Directors held during the year ended 30 June 2009 and attended by each Director.

	Board meetings		Audit meetings	
	Held	Attended	Held	Attended
	while a Director		while a member	
R Warburton	4	4		
J Ballard	4	4	6	6
A Hogendijk	4	4	6	6
C Mackay	4	4	6	6
H Douglass	4	4		

REMUNERATION REPORT (AUDITED)

Principles used to determine the nature and amount of remuneration
The Non-Independent Directors (Mr Mackay and Mr Douglass) review and determine the remuneration of the Independent Non-Executive Directors and may utilise the services of external advisors. It is the policy of the Board to remunerate at market rates commensurate with the responsibilities borne by the Non-Executive Directors. The remuneration of the Directors is not linked to the performance or earnings of the Company.

Directors' fees
Non-Executive Directors' base remuneration is reviewed annually.

Retirement benefits for Directors
No retirement benefits (other than superannuation) are provided to Directors.

Other benefits (including termination) and incentives
No other benefits and incentives are paid to Directors.

Details of Remuneration
Only the Independent Non-Executive Directors were remunerated by the Company and received the following amounts during the year:

	30 June 2009			30 June 2008		
	Short term Benefits (Salary)	Post-employment Benefits Superannuation	Total	Short term Benefits (Salary)	Post-employment Benefits Superannuation	Total
	$	$	$	$	$	$
R Warburton	77,982	7,018	85,000	77,982	7,018	85,000
J Ballard	28,670	33,830	62,500	42,000	20,500	62,500
A Hogendijk	68,807	6,193	75,000	68,807	6,193	75,000

DIRECTORS' REPORT (CONTINUED)

The Non-Independent Directors (Mr Mackay and Mr Douglass) are both employees of the Investment Manager and are not remunerated by the Company. The Non-Independent Directors received the following amounts from the Investment Manager during the year:

	30 June 2009			30 June 2008		
	Short term Benefits (Salary)	Post-employment Benefits Superannuation	Total	Short term Benefits (Salary)	Post-employment Benefits Superannuation	Total
	$	$	$	$	$	$
C Mackay	236,255	13,745	250,000	78,957	5,059	84,016
H Douglass	236,255	13,745	250,000	78,957	5,059	84,016

A portion of the remuneration paid by the Investment Manager to Mr Mackay and Mr Douglass is in relation to managing the affairs of the Company. The Investment Manager has made no determination as to what proportion of Mr Mackay's and Mr Douglass' remuneration is related to the Company. The Non-Independent Directors were remunerated from 1 March 2008 by the Investment Manager.

KEY MANAGEMENT PERSONNEL COMPENSATION

Key management personnel include persons and corporate entities having authority and responsibility for planning, directing and controlling activities of the Company. The Company has no employees other than its Directors whose remuneration is disclosed above.

The Investment Manager is a corporate entity that has specified authority and responsibility in regard to the Company and is remunerated by the Company as disclosed in note 11 to the financial statements. The Investment Manager does not directly or indirectly own shares in the Company. At the date of this report the parent company of the Investment Manager, Magellan Financial Group Limited (MFG), owns 44,727,166 or 12.49% (2008: 27,494,268 or 7.27%,) of the Company's shares.

SHARE HOLDINGS

The number of ordinary shares in which the Directors have a relevant interest at balance date is as follows:

Name	Balance at 1 July 2008	Acquisitions	Disposals	Balance at 30 June 2009
Richard Warburton	650,000	-	-	650,000
John Ballard	1,100,000	-	-	1,100,000
Andy Hogendijk	125,000	-	-	125,000
Chris Mackay *	14,515,128	4,399,171	-	18,914,299
Hamish Douglass *	750,000	-	-	750,000

None of the Directors' or MFG's holdings in the Company are subject to margin loan arrangements.

* Mr. Mackay and Mr. Douglass are also Directors of MFG, which owned 30,391,049 shares in the Company at 30 June 2009 (2008: 27,494,268 shares, including shares held by MFG's controlled entity, NPH). As at the date of this report, MFG's shareholding had been increased to 44,727,166 shares in the Company.

SERVICE AGREEMENTS

Remuneration and other terms of employment for the Independent Non-Executive Directors are formalised in service agreements. The Non-Independent Directors do not have service agreements with the Company.

Richard Warburton AO, Chairman and Independent Non-Executive Director

- Commenced on 19 October 2006
- No term of agreement has been set unless the Director is not re-elected by Shareholders of the Company
- Base salary, inclusive of superannuation, for the year ended 30 June 2009 of $85,000.

John Ballard, Independent Non-Executive Director

- Commenced on 19 October 2006
- No term of agreement has been set unless the Director is not re-elected by Shareholders of the Company
- Base salary, inclusive of superannuation, for the period ended 30 June 2009 of $62,500

Andy Hogendijk, Independent Non-Executive Director and Chairman of the Audit and Risk Committee

- Commenced on 19 October 2006
- No term of agreement has been set unless the Director is not re-elected by Shareholders of the Company
- Base salary, inclusive of superannuation, for the period ended 30 June 2009 of $75,000

Chris Mackay, Non-Independent Non-Executive Director

- Commenced on 29 September 2006
- No term of agreement has been set unless the Director is not re-elected by shareholders of the Company
- No Base salary or other compensation from the Company

Hamish Douglass, Non-Independent Non-Executive Director

- Commenced on 29 September 2006
- No term of agreement has been set unless the Director is not re-elected by shareholders of the Company
- No Base salary or other compensation from the Company

SHARED BASED COMPENSATION

No shares or options have been granted to Directors or to the key management personnel.

DIRECTORS' INTERESTS IN CONTRACTS

The Non-Independent Directors of the Company are Directors and employees of, and have a relevant interest in, the Investment Manager. They do not receive any Directors' remuneration from the Company.

DIRECTORS AND OFFICERS' INSURANCE

The Company has paid premiums to insure each of its Directors and Officers in office against liabilities for costs and expenses incurred by them in defending any legal proceedings arising out of their conduct while acting in the capacity of Directors and Officers of the Company, other than conduct involving a wilful breach of duty in relation to the Company.

This report is made in accordance with a resolution of the Directors.

Richard Warburton AO
Chairman
Sydney
26 August 2009

AUDITOR'S INDEPENDENCE DECLARATION

ERNST & YOUNG

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Auditor's Independence Declaration to the Directors of Magellan Flagship Fund Limited

In relation to our audit of the financial report of Magellan Flagship Fund Limited for the financial year ended 30 June 2009, to the best of my knowledge and belief, there have been no contraventions of the auditor independence requirements of the *Corporations Act 2001* or any applicable code of professional conduct.

Ernst & Young

Ernst & Young

R Da Silva

Rita Da Silva
Partner
26 August 2009

CORPORATE GOVERNANCE STATEMENT

FOR THE YEAR ENDED 30 JUNE 2009

Magellan Flagship Fund Limited (the "Company") is a listed investment Company whose shares are traded on the Australian Securities Exchange (ASX). The Board and Management of the Company recognise the importance of good corporate governance. The Company's corporate governance framework, policies and practices are designed to ensure the effective management and operation of the Company, and will remain under regular review.

1. THE BOARD

1.1 The Board of Directors

R. Warburton A.O (Chairman, Independent Non-Executive Director)
J. Ballard (Independent Non-Executive Director)
A. Hogendijk (Independent Non-Executive Director)
C. Mackay (Non-Executive Director)
H. Douglass (Non-Executive Director)

Details of each Board member's background and attendance at Board meetings are set out in the Directors' Report.

The Board is responsible for the overall operation and stewardship of the Company and is responsible for its overall success and long-term growth and corporate governance. The Board will act in the best interests of the Company to ensure the business of the Company is properly managed.

1.2 Board Composition and Independence

There must be a minimum of three Directors and a maximum of ten Directors. The Board has a majority of Independent Non-Executive Directors.

The Board must comprise:
- Directors with an appropriate range of skills, experience and expertise;
- Directors who can understand and competently deal with current and emerging business issues; and
- Directors who can effectively review and challenge the performance of the Investment Manager and exercise independent judgment.

The Board currently comprises five Non-Executive Directors, three of whom are Independent Non-Executive Directors.

A Director must retire from office no later than the later of the third annual general meeting of the Company or three years following the Director's last election or appointment.

An Independent Non-Executive Director is a non-executive Director who is independent of the Investment Manager and free of any business or other relationship that could materially interfere with, or could reasonably be perceived to materially interfere with, the exercise of their unfettered and independent judgment.

The Board is confident that each of the Directors will bring skills and qualifications to the Company which will enable them to effectively discharge their individual and collective responsibilities as Directors of the Company.

The Board considers that the number of Directors is sufficient to enable it to effectively discharge its responsibilities. However, the composition of the Board will be reviewed periodically and its independence, and that of the individual Directors, will be assessed as part of those reviews.

The Board has authorised the Investment Manager to make decisions concerning the Company but has expressly reserved certain matters requiring a decision of the Board.

1.3 The Role of the Board and Delegation

The Company's corporate governance policies revolve around its Board Charter, the purpose of which is to:

- promote high standards of corporate governance;
- clarify the role and responsibilities of the Board; and
- enable the Board to provide strategic guidance for the Company and effective operational oversight.

The Board Charter will apply subject to applicable legal and regulatory requirements, including duties and obligations imposed on the directors by statute and general law. The Board may review and amend the Board Charter at any time. The Board Charter is available from the Company by contacting the Company Secretary.

The principal responsibilities of the Board include:

- assessing the Company's overall performance;
- reporting to shareholders;
- exercising all rights conferred on it and performing all obligations imposed on it under the Investment Management Agreement;
- reviewing at regular intervals relevant aspects of the Investment Management Agreement;
- reviewing and having input into overall target portfolio composition;
- providing strategic guidance to the Investment Manager on investments;
- monitoring and assessing the performance of the Investment Manager under the Investment Management Agreement;
- reviewing at regular intervals relevant aspects of the Administrative Services Agreement;
- monitoring and assessing the performance of the Investment Manager under the Administrative Services Agreement;
- monitoring and ensuring compliance with best practice corporate governance requirements; and
- ensuring the risk management systems, including internal controls, operating systems and compliance processes, are operating efficiently and effectively.

Subject to legal or regulatory requirement and the Company's Constitution, the Board may delegate any of the above powers to individual directors, committees of the Board or the Investment Manager. Any such delegation shall be in compliance with the law and the Company's Constitution.

1.4 Non-Executive Directors' remuneration structure

The Independent Non-Executive Directors' fees are $85,000 per annum for the Chairman, $50,000 per annum for each Director, and an additional $25,000 per annum for the Chairman, and $12,500 per annum for each other member, of the Audit and Risk Committee, plus in each case reimbursement of expenses such as travelling expenses.

The Non-Independent Directors, Chris Mackay and Hamish Douglass, did not receive any fees in relation to acting as Directors of the Company or, in the case of Chris Mackay, as a member of the Audit and Risk Committee.

The maximum aggregate sum fixed for payment of the total non-executive Directors' fees is $500,000 per annum until the shareholders, by an ordinary resolution, approve some other fixed sum. This amount is to be divided amongst the Directors as they may determine.

1.5 Evaluation of Performance

The Board reviews its performance in terms of Company objectives, Company results and achievements of the Investment Manager. The Company has no employees and a result, the evaluation of the performance of senior executives is not applicable. This represents a departure from Recommendations 1.2 and 1.3 of the ASX Principles as the Company has not disclosed the process for the evaluation of the performance of senior executives.

1.6 Access to Information and Independent Advice

Directors have access to any information they consider necessary to fulfil their responsibilities and to exercise independent judgment when making decisions.

Directors may obtain independent professional advice at the Company's expense, subject to making a request to, and obtaining the prior authorisation of, the chairperson of the Board. Where the chairperson of the Board wishes to obtain independent professional advice, he or she is required to make a request to, and obtain the prior authorisation of, the chairperson of the Audit and Risk Committee of the Board.

2. BOARD COMMITTEES

The Board may from time to time establish committees to assist it in the discharge of its responsibilities. To date, the Board has only found a need to establish the Audit and Risk Committee. Other committees may be established by the Board as and when required. Membership of Board committees will be based on the needs of the Company, relevant legislative and other requirements and the skills and experience of individual Directors. The Board expects that, over time, the Directors will rotate on and off various committees. Committee members will be appointed for a three year term of office. The Company does not have a Nomination Committee. This represents a departure from Recommendations 1.2 and 1.3 of the ASX Principles as a Nomination Committee is not required given the size and nature of the Company.

Performance of all committee members will be reviewed periodically by the Board.

Audit and Risk Committee

The Audit and Risk Committee is comprised of:

- A. Hogendijk (Chair, Independent Non-Executive Director)
- J. Ballard (Independent Non-Executive Director)
- C. Mackay (Non-Executive Director)

Details of each Committee member's background and attendance at Audit and Risk Committees are set out in the Directors' Report.

The Chairman of the Audit and Risk Committee is an Independent Non-Executive Director and is not the Chairman of the Board.

The objective of the Audit and Risk Committee is to assist the Board to discharge its responsibilities in relation to:

- effective management of financial and operational risks;
- compliance with laws and regulations;
- accurate management and financial reporting;
- maintenance of an effective and efficient audit; and
- high standards of business ethics and corporate governance.

These objectives form the foundation of the Audit and Risk Committee's Charter. A copy of this Charter is available from the Company by contacting the Company Secretary.

The Audit and Risk Committee will endeavour to:

- maintain and improve the quality, credibility and objectivity of the financial accountability process;
- promote a culture of compliance within the Company;
- ensure effective communication between the Board, the Investment Manager and the Investment Manager's senior financial and compliance management;
- ensure effective audit functions and communications between the Board and the Company auditor;
- ensure that compliance strategies and compliance functions are effective; and
- ensure that Directors are provided with financial and non-financial information that is of high quality and relevant to the judgments to be made by them.

3. ETHICAL CONDUCT

The Company has a Corporate Code of Conduct (the "Code") that applies to Directors of the Company and to Directors and employees of the Investment Manager. The purpose of this Code is to:

(a) articulate the high standards of honest, ethical and law-abiding behaviour that the Company expects of its Directors and the Directors and employees of the Investment Manager;
(b) encourage the observance of those standards so as to protect and promote the interests of shareholders and other stakeholders;
(c) guide the Company's Directors and the Directors and employees of the Investment Manager as to the practices thought necessary to maintain confidence in the Company's integrity; and
(d) set out the responsibilities and accountabilities of Directors and employees of the Investment Manager to report and investigate reports of unethical practices.

A copy of the Corporate Code of Conduct is available from the Company by contacting the Company Secretary.

4. MARKET DISCLOSURE

The Company is committed to complying with its continuous disclosure obligations under the Corporations Act 2001 and the Listing Rules, as well as releasing relevant information to the market and shareholders in a timely and direct manner and to promoting investor confidence in the Company and its securities.

The Board has adopted a Continuous Disclosure Policy that is designed to ensure that the Company:

- as a minimum complies with its continuous disclosure obligations under the Corporations Act 2001 and the ASX Listing Rules;
- provides shareholders and the market with timely, direct and equal access to information issued by it; and
- that information which is not generally available and which may have a material effect on the price or value of the Company securities (price sensitive information), be identified and appropriately considered by the Directors and senior executives for disclosure to the market.

The Policy, which is available from the Company by contacting the Company Secretary, also sets out procedures which must be followed in relation to releasing announcements to the market and discussions with analysts, the media or shareholders.

The Company market announcements will also be available its website after they are released to ASX.

5. SHAREHOLDER COMMUNICATIONS

The Board is committed to ensuring that shareholders are fully informed of material matters that affect the Company's position and prospects. It seeks to accomplish this through a strategy which includes:

- the Half Year Results released in February each year;
- the Full Year Results released in August each year;
- the Chairman's Letter to Shareholders each year;
- the Annual Report released in September each year;
- the Chairman's and Chief Investment Officer's addresses to the Annual General Meeting;
- the posting of the Company's weekly and Monthly NTA on the Company's website as soon as it is disclosed to the market; and
- the posting of significant information on the Company's website as soon as it is disclosed to the market.

The Company holds its Annual General Meeting in October and a copy of the notice of Annual General Meeting is posted on the Company's website and mailed to shareholders. The Board encourages shareholders to attend the Annual General Meeting or to appoint a proxy to vote on their behalf if they are unable to attend. The formal addresses at the Annual General Meeting are disclosed to the market.

The Company's external auditor will be invited to attend any annual meeting and will be available to answer questions about the conduct of the audit and the preparation and contents of the auditor's report.

6. SHARE TRADING

The Board has adopted a policy which sets out the circumstances in which Directors of the Company and Directors and employees of the Investment Manager may deal in:

- the Company's securities, which includes any shares in the Company, debentures (including convertible notes) issued by the Company and options to acquire or subscribe for shares in the Company; and
- other financial products, which includes any shares, options, derivatives (including market index derivatives), debentures any other financial product able to be traded of any company, trust or other organisation, local domestic and international, in which the Company invests or proposes to invest,

with the objective that no Director or employee will contravene the requirements of the Corporations Act 2001, the ASX Listing Rules or any other applicable law.

The purpose of this policy is designed to protect the reputation of the Company and to ensure that such reputation is maintained or perceived to be maintained by persons external to the Company.

An overriding principle of the policy is that the Directors and employees who possess non-public price sensitive information must not deal in the Company's securities.

A copy of the Company's Trading Policy is available from the Company by contacting the Company Secretary.

7. RISK MANAGEMENT

The Board, through the Audit and Risk Committee, is responsible for ensuring that:

- there are adequate policies for the oversight and management of material business risks to the Company;
- there are effective systems in place to identify, assess, monitor and manage the risks of the Company and to identify material changes to the Company's risk profile; and
- arrangements are adequate for monitoring compliance with laws and regulations applicable to the Company.

CORPORATE GOVERNANCE STATEMENT (CONTINUED)
FOR THE YEAR ENDED 30 JUNE 2009

Risks assessed include:

- implementing strategies (strategic risk);
- operations or external events (operational risk);
- legal and regulatory compliance (legal risk);
- changes in community expectation of corporate behaviour (reputation risk); and
- being unable to fund operations or convert assets into cash (liquidity risk).

The Investment Manager, Magellan Asset Management Limited, has implemented risk management and compliance frameworks. These frameworks ensure that:

- emphasis is placed on maintaining a strong control environment;
- accountability and delegations of authority are clearly identified;
- risk profiles are in place and are regularly reviewed and updated;
- timely and accurate reporting is provided to Management and respective Committees; and
- compliance with the law, contractual obligations and internal policies (including business rules of conduct) is communicated and demonstrated

The Investment Manager reports periodically to the Audit and Risk Committee on the effectiveness of its risk management and compliance frameworks with respect to services undertaken for the Company.

8. CORPORATE REPORTING

In respect of the year ending 30 June 2009 the Chief Investment Officer and Chief Financial Officer of the Investment Manager have made the following certifications to the Board:

- the financial records of the Company for the financial period have been properly maintained in accordance with section 286 of the Corporations Act 2001 (Act);
- the financial statements and notes referred to in paragraph 295(3)(b) of the Act for the financial period comply with the accounting standards;
- the financial statements and notes for the financial period give a true and fair view (as per section 297 of the Act);
- any other matters that are prescribed by the Corporations Regulations in relation to the financial statements and the notes for the financial period are satisfied;
- the integrity of the Company's financial statements is founded on a sound system of risk management and internal compliance and control which implements the policies adopted by the Board; and
- the Company's risk management and internal compliance and control system is operating efficiently and effectively in all material respects.

9. REMUNERATION

The Investment Manager is entitled to be paid management and performance fees in accordance with the Investment Management Agreement between the Company and the Investment Manager.

Persons involved in management the of the Company's portfolio are employees of the Investment Manager and are not remunerated by the Company. As the Company does not pay any remuneration to executives, the Company considers that the requirement to disclose its remuneration policies and to establish a remuneration committee are not relevant to the Company. This represents a departure from the ASX Recommendation 8.1 and 8.3, as the Manager has not established a remuneration committee.

INCOME STATEMENT

FOR THE YEAR ENDED 30 JUNE 2009

	Note	30 June 2009 $ '000	30 June 2008 $ '000
Investment income			
Dividend income		8,596	6,471
Interest income		190	1,882
Net changes in fair value of investments		(15,402)	(107,755)
Net losses on foreign currency borrowings		(8,517)	(4,439)
Net gains on foreign exchange		1,033	642
Other income		13	-
Total investment loss		**(14,087)**	**(103,199)**
Expenses			
Management fees		3,226	3,932
Finance costs – interest expense		1,587	1,130
Directors' fees		223	225
Auditors remuneration		102	66
Transaction costs		89	98
Registry fees		46	99
Fund administration fees		48	43
Listing and chess fees		35	41
Legal and professional fees		28	33
Other expenses		68	124
Total operating expenses		**5,452**	**5,791**
Loss before income tax		**(19,539)**	**(108,990)**
Income tax benefit	2(a)	4,808	32,697
Net loss after income tax		**(14,731)**	**(76,293)**
		Cents per Share	
Basic loss per share	6	**(3.96)**	**(20.18)**
Diluted loss per share	6	**(3.96)**	**(20.18)**

The Income Statement should be read in conjunction with the accompanying notes.

BALANCE SHEET

AS AT 30 JUNE 2009

	Note	30 June 2009 $ '000	30 June 2008 $ '000
Current assets			
Cash and cash equivalents	7(a)	54	112
Investments at market value	3	277,264	306,829
Receivables	4	682	654
Prepayments		14	82
Total current assets		**278,014**	**307,677**
Non-current assets			
Deferred tax assets	2(d)	42,813	36,879
Total non-current assets		**42,813**	**36,879**
Total assets		**320,827**	**344,556**
Current liabilities			
Borrowings	7(b)	47,044	49,227
Payables	5	833	890
Total current liabilities		**47,877**	**50,117**
Total liabilities		**47,877**	**50,117**
Net assets		**272,950**	**294,439**
Equity			
Contributed equity	8	366,822	373,580
Accumulated loss		(93,872)	(79,141)
Total equity		**272,950**	**294,439**

The Balance Sheet should be read in conjunction with accompanying notes.

STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 30 JUNE 2009

	30 June 2009 $ '000	30 June 2008 $ '000
Contributed equity		
Balance at beginning of year	373,580	373,580
Shares acquired under buy-back	(6,746)	-
Transaction costs on share buy-back	(17)	-
Transaction costs on share buy-back – tax effect	5	-
Balance at end of year	**366,822**	**373,580**
Accumulated loss		
Balance at beginning of year	(79,141)	(2,848)
Net loss after income tax for the year	(14,731)	(76,293)
Balance at end of year	**(93,872)**	**(79,141)**
Total equity	**272,950**	**294,439**

The Statement of Changes in Equity should be read in conjunction with accompanying notes.

STATEMENT OF CASH FLOWS

FOR THE YEAR ENDED 30 JUNE 2009

	Note	30 June 2009 $ '000	30 June 2008 $ '000
Cash flows from operating activities			
Dividends received	7(c)	6,788	5,312
Interest received		190	1,882
Other income received		9	-
Payments for purchase of investments		(79,857)	(182,289)
Proceeds from sale of investments		94,546	52,919
Net foreign exchange gains		1,033	642
Management fees paid		(3,311)	(4,280)
Other expenses paid		(444)	(790)
Net cash inflow/(outflow) from operating activities	7(d)	**18,954**	**(126,604)**
Cash flows from financing activities			
Net proceeds / (repayment) on borrowings		(10,700)	44,788
Interest paid		(1,587)	(1,130)
Payment for shares under buy-back		(6,708)	-
Payment of share buy-back costs		(17)	-
Net cash (outflow)/inflow from financing activities		**(19,012)**	**43,658**
Net decrease in cash and cash equivalents		(58)	(82,946)
Cash and cash equivalents at the beginning of the year		112	83,058
Cash and cash equivalents at the end of the year	7(a)	**54**	**112**

The Statement of Cash Flows should be read in conjunction with accompanying notes.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2009

1. Summary of Significant Accounting Policies

Basis of Preparation

This financial report is a general purpose financial report which has been prepared in accordance with the *Corporations Act 2001*, and Australian Accounting Standards. The financial report has been prepared under the historical cost convention except for investments which are measured at fair value.

The principal accounting policies adopted in the preparation of the financial report are set out below. These policies have been consistently applied to the years presented, unless otherwise stated.

(a) Compliance with IFRS

The financial report complies with Australian Accounting Standards as issued by the Australian Accounting Standards Board and International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board.

The preparation of the financial statements in conformity with IFRS requires the use of certain critical accounting estimates and judgements, which are included below.

(b) Income Tax

The income tax expense or benefit for the year is the tax payable or receivable on the current year taxable income or loss based on the current income tax rate adjusted by changes in deferred tax assets and liabilities attributable to temporary differences between the tax bases of assets and liabilities and their carrying amounts in the financial statements, and to unused tax losses. Under AASB 112: *Income Taxes,* deferred tax balances are determined using the Balance Sheet method which calculates temporary differences based on the carrying amounts of an entity's assets and liabilities in the Balance Sheet and their associated tax bases.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

(c) Investments at Market Value

Under AASB 139: *Financial Instruments: Recognition and Measurement*, investments are classified in the Balance Sheet as "held at fair value through profit and loss". Investments at market value are initially recognised at fair value, typically represented by cost excluding transaction costs, which are expensed as incurred.

Investments at market value designated at fair value through profit and loss are revalued to fair value at each reporting date as follows:

- securities and rights to them listed on a financial market – valued at the market value based on bid prices as quoted on the relevant exchange

Investments have been designated as held at fair value through profit or loss as doing so results in more relevant information. Investments are managed collectively and their performance is evaluated on a fair value basis in accordance with the investment strategies and risk management policies of the Company.

(d) Transaction Costs

Initial measurement (cost) on acquisition of trading securities does not include directly attributable transaction costs such as fees and commissions paid to agents. Incremental transaction costs are expensed as incurred in the Income Statement.

(e) Foreign Currency Translation

The functional and presentation currency of the Company as determined in accordance with AASB 121: *The Effects of Changes in Foreign Exchange Rates* is the Australian dollar.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 30 JUNE 2009

1. Summary of Significant Accounting Policies (continued)

(e) Foreign Currency Translation (continued)

Transactions denominated in foreign currencies are translated into Australian currency at the foreign currency exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated to Australian Dollars at the foreign currency closing exchange rate ruling at the balance sheet date.

Foreign currency exchange differences arising on translation and realised gains and losses on disposals or settlements of monetary assets and liabilities are recognised in the Income Statement. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are translated to Australian dollars at the foreign currency closing exchange rates ruling at the dates that the values were determined. Foreign currency exchange differences relating to monetary items, including cash and cash equivalents, are presented separately in the Income Statement.

(f) Investment Income

Dividend income
Dividend income is recognised on the applicable ex-dividend date.

Gains and losses on investments "designated as held at fair value through profit & loss".
Unrealised gains and losses on investments designated at fair value through profit or loss are recognised in the Income Statement.

(g) Directors' Entitlements
Liabilities for Directors' entitlements to fees are accrued at nominal amounts calculated on the basis of current fee rates. Contributions to Directors' superannuation plans are charged as an expense as the contributions are paid or become payable.

(h) Earnings Per Share
Basic and diluted earnings per share are determined by dividing the operating profit / (loss) after income tax by the weighted number of ordinary shares outstanding during the financial year.

(i) Cash and Cash Equivalents
For cash flow statement presentation purposes, cash and cash equivalents includes cash on hand,
deposits held at call with financial institutions, other short term, highly liquid investments with original maturities of three months or less that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value net of borrowings.

Payments and receipts relating to the purchase and sale of investment securities are classified as cash flows from operating activities, as movements in the fair value of these securities represent the Company's main income generating activity.

(j) Receivables
Receivables are recognised as and when they are due.

Debts which are known to be uncollectible are written off. A provision for doubtful debts is raised when there is evidence the amount will not be collected.

(k) Payables
Payables and trade creditors are recognised as and when they are incurred. Payables on purchase of investments are usually paid between two and five days after trade date. Trade creditors are unsecured and payable between seven and 30 days after being incurred. Payables are non-interest bearing.

(l) Contributed Equity
Ordinary shares are classified as equity.

(m) Rounding of Amounts
The Company is an entity of the kind referred to in Class Order 98/0100 (as amended), issued by the Australian

Securities and Investments Commission, relating to the ''rounding off'' of amounts in the financial report. Amounts in the financial report have been rounded off to the nearest thousand dollars in accordance with that Class Order, unless otherwise indicated.

(n) Goods and Services Tax (GST)
Revenue, expenses and assets recognised net of the amount of any GST except when GST incurred on a purchase of goods and services is not recoverable from the taxation authority, in which case the GST is recognised as part of the cost of that purchase.

(o) New Accounting Standards and Interpretations
Certain new accounting standards and interpretations have been published that are not mandatory for 30 June 2009 reporting year. The directors' assessment of the impact of these new standards (to the extent relevant to the Company) and interpretations is set out below:

(i) AASB 8 *Operating Segments* and AASB 2007-3 *Amendments to Australian Accounting Standards arising from* AASB 8.

AASB 8 and AASB 2007-3 are effective for annual reporting years beginning on or after 1 January 2009. The Company has not adopted these standards early. Application of these standards will not affect any of the amounts recognised in the financial statements, but may affect the segment disclosures provided in note 13.

(ii) Revised AASB 101 *Presentation of Financial Statements* and AASB 2007-8 *Amendments to Australian Accounting Standards arising from* AASB 101.

AASB 101 (Revised) is applicable to annual reporting years beginning on or after 1 January 2009. The Company has not adopted this standard early. It requires the presentation of a statement of comprehensive income and makes changes to the statement of changes in equity but will not affect any of the amounts recognised in the financial statements. If the Company makes a prior year adjustment or re-classifies items in the financial statement, it will need to disclose a third balance sheet (statement of financial position), this one being at the beginning of the comparative year.

(p) Comparative Information
Net foreign exchange losses on investments quoted in foreign currencies were previously included in 'Net losses on foreign exchange' on the face of the Income Statement. These foreign exchange losses have been aggregated into 'Net change in fair value of investments' to reflect disclosure more consistent with industry peers and accounting standards.

'Net losses on foreign currency borrowings' and 'Net gains on foreign exchange' were previously included in 'Net losses on foreign exchange' on the face of the Income Statement. For year end reporting these lines have been separately disclosed.

Cash and cash equivalents in the prior year Statement of Cash Flows was reported as cash and cash equivalents, net of borrowings – refer to note 7a) and 7b). Cash and cash equivalents in the current year Statement of Cash Flows comprises only cash and cash equivalents.

The prior year comparatives have been reclassified accordingly.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 30 JUNE 2009

2. INCOME TAX

	30 June 2009	30 June 2008
	$ '000	$ '000
(a) The income tax benefit attributable to the financial year differs from the prima facie amount payable on the operating loss. The difference is reconciled as follows:		
Loss before income tax expense	(19,539)	(108,990)
Prima facie income tax benefit on the operating loss at 30%	5,861	32,697
Tax effect of franked dividends received	(69)	-
Write-off of deferred income tax benefit on foreign tax paid[1]	(1,069)	-
Over provision of prior year tax	85	-
	4,808	**32,697**
(b) The major components of income tax expense are:		
Current income tax benefit / (expense)	1,790	25
Deferred income tax benefit / (expense)		
– origination and reversal of temporary differences	4,002	32,672
– write-off of deferred income tax benefit on foreign tax paid[1]	(1,069)	-
Over provision of prior year tax	85	-
	4,808	32,697
(c) Income tax benefits / (charge) directly to equity:		
Costs associated with the issue / buy-back of shares	(5)	-
	(5)	-
(d) Deferred tax assets relate to the following:		
Tax losses carried forward	2,021	143
Capital losses carried forward	11,334	-
Costs associated with the issue / buy-back of shares	762	1,137
Unrealised loss on investments	27,744	34,424
Allowable tax credits	1,118	1,067
Other temporary differences	(166)	108
	42,813	36,879

In the Directors' judgement the future earnings potential and underlying business economics of the investee companies are favourable and, as the Company possesses the ability and intent to hold these investments until their prices recover, it is probable that future taxable amounts will be available to offset these deferred tax assets within generally acceptable timeframes.

[1] From 1 July 2008 changes to the foreign tax credit regime have resulted in foreign tax withheld on foreign dividends being only off-settable against taxable income in the related tax year. As a result of this change and the Company being in a tax loss position, current year foreign tax credits have been written off during the financial year.

3. INVESTMENTS AT MARKET VALUE

	Domicile of Principal Exchange Listing	30 June 2009 $ '000	30 June 2008 $ '000
American Express Company *	United States	39,885	52,034
Nestlé *	Switzerland	34,375	32,346
Yum Brands *	United States	34,046	28,725
Wal-Mart Stores *	United States	28,712	25,761
eBay *	United States	21,273	28,605
PepsiCo *	United States	18,273	15,200
Google *	United States	13,088	1,646
Coca-Cola *	United States	12,754	244
Procter & Gamble *	United States	11,457	4,987
McDonald's *	United States	9,917	29
Tesco *	United Kingdom	9,029	8,342
Colgate-Palmolive Co *	United States	7,115	-
Unilever *	Netherlands	6,481	12,609
Bank of America	United States	6,069	10,808
Lowe's	United States	4,495	7,893
Johnson & Johnson *	United States	4,033	10,537
Visa *	United States	3,898	-
Cintra *	Spain	2,010	3,064
Mastercard Inc *	United States	1,678	-
US Bancorp	United States	1,665	6,481
SLM Corp	United States	-	15,763
ASX	Australia	-	9,106
Home Depot	United States	-	5,255
Total top 20 holdings		**270,253**	**279,435**
Other companies		7,011	27,394
Total listed securities		**277,264**	**306,829**

* Entities that generate 50% or more of their revenue and / or have operations in 15 or more countries outside of the country of domicile of their primary securities exchange

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 30 JUNE 2009

3. INVESTMENTS AT MARKET VALUE (CONTINUED)

The following table illustrates changes in Australian dollar exchange rates against the following currencies (London 4.00pm rates):

	30 June 2009	30 June 2008
	$	$
US Dollars	0.8084	0.9597
Euros	0.5764	0.6091
British Pounds	0.4909	0.4822
Swiss Francs	0.8792	0.9775

4. RECEIVABLES

	30 June 2009	30 June 2008
	$ '000	$ '000
Dividends receivable	612	261
Foreign tax recoverable	17	200
Goods and Service Tax	53	193
Total receivables	**682**	**654**

Denomination of current receivables by currency:

Australian Dollars	92	219
US Dollars	359	89
Euros	17	19
Swiss Francs	-	182
British Pounds	214	145
	682	654

5. PAYABLES

	30 June 2009	30 June 2008
	$ '000	$ '000
Accrued expenses	723	807
Trade payable	110	83
Total payables	**833**	**890**
Denomination of current payables by geographic location:		
Australian Dollars	833	890
	833	890

6. EARNINGS PER SHARE

	30 June 2009	30 June 2008
Basic loss per shares (cents)	(3.96)	(20.18)
Diluted loss per shares (cents)	(3.96)	(20.18)
Weighted average number of ordinary shares on issue used in the calculation of basic and diluted earnings per share	371,809,533	378,000,005
Loss used in the calculation of basic and diluted earnings per share ($'000)	(14,731)	(76,293)

As there are no potential ordinary shares, diluted loss per share is equal to basic loss per share.

7. NOTES TO THE STATEMENT OF CASH FLOWS

(a) Current asset - Cash and cash equivalents - cash

	30 June 2009	30 June 2008
	$ '000	$ '000
Cash – cash denominated in AUD	54	112
	54	112

All accounts are at call and are at floating interest rates.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 30 JUNE 2009

7. NOTES TO THE STATEMENT OF CASH FLOWS (CONTINUED)

(b) Current liability – Interest bearing borrowings

	30 June 2009	30 June 2008
	$ '000	$ '000
Borrowings – denominated in AUD	(29,585)	(135)
Borrowings – denominated in CHF	(1,013)	-
Cash – denominated in USD	1,940	(12,017)
Borrowings - denominated in GBP	(10,088)	(9,200)
Borrowings – denominated in EUR	(8,298)	(27,875)
	(47,044)	**(49,227)**

The Company's borrowings are under a multi-currency financing facility with Merrill Lynch (refer note 14). Foreign currency cash balances held with Merrill Lynch are netted against foreign currency borrowings.

(c) Dividends received

Foreign dividends received are net of foreign taxes withheld. Shares received under Dividend Reinvestment Plans are non-cash items.

(d) Reconciliation of net loss after income tax to net cash from operating activities

Net loss after income tax	(14,731)	(76,293)
Foreign exchange loss on repayment of borrowings and from transacting in foreign currencies	8,517	4,439
Interest expense	1,587	1,130
Decrease/(increase) in investments at market value	29,565	(19,743)
Increase in dividends receivable	(351)	(154)
Decrease/(increase) in withholding tax receivables	183	(142)
Decrease/(increase) in GST receivables	140	(44)
Decrease/(increase) in prepayments	68	(42)
Decrease in unsettled trades payable	-	(1,872)
Decrease in management fee payable	(84)	(348)
(Decrease)/increase in trade payables and accrued expenses	(6)	25
Increase in deferred tax	(5,934)	(33,560)
Net cash inflow/(outflow) from operating activities	**18,954**	**(126,604)**

8. CONTRIBUTED EQUITY

	30 June 2008	30 June 2007
	$ '000	$ '000
Balance at beginning of the year	373,580	373,580
Shares cancelled under share buy-back	(6,758)	-
Balance at end of the year	**366,822**	**373,580**

Fully paid ordinary shares carry one vote per share and carry the right to dividends.
At 30 June 2009 365,573,153 ordinary shares were on issue (2008: 378,000,005). 12,426,852 shares were cancelled during the year under the share buy-back as described in the Directors' Report.

9. STATEMENT OF NET ASSET VALUE

	30 June 2009	30 June 2008
Reconciliation of Net Asset Value to the ASX		
Net Asset Value per Balance Sheet $'000	272,950	294,439
Divided by:		
Number of shares on issue	365,573,153	378,000,005
Net Asset Value – cents per share	**75**	**78**
Net Asset Value – ASX announcement 2 July 2009 – cents per share	**75**	**78**

10. RISK MANAGEMENT

The Company's investment portfolio comprises listed equity securities. It is the Company's investment objective to seek long term capital growth by investing in listed international and Australian companies with attractive business characteristics at discounts to their assessed intrinsic values.

The Company's investing activities expose it to various types of risk that are associated with the financial instruments and markets in which it invests. The most important types of financial risk to which the Company is exposed are price risk, currency risk, credit risk and liquidity risk.

The Company has investment restrictions designed to reduce risk, including the requirement that, individual investments comprising the investment portfolio will not exceed 20% of the investment portfolio value of the Company at the time of the investment.

The Company has a policy that at the time any new borrowings are entered into the aggregate of those new borrowings and any pre-existing borrowings must not exceed 20% of the investment portfolio value. The use of derivatives is very limited and permitted only where the Investment Manager considers that a derivative is preferable to purchasing ordinary share capital, in accordance with the investment objectives and philosophy. Short selling activity is very limited and permitted only in relation to implementing hedges of underlying investments or merger arbitrage relating to a portfolio investment. The use of derivatives and short selling did not occur during the year ended 2009.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 30 JUNE 2009

10. RISK MANAGEMENT (CONTINUED)

(a) Market Risk

Price Risk
Price risk is the risk that the value of the Company's investment portfolio will fluctuate as a result of changes in market prices of individual investments and / or the market as a whole. The Company's investments are carried at market value with changes recognised in the Income Statement and directly affect net investment income. Price risk is managed by ensuring that all activities are transacted in accordance with the Company's investment policy and within approved limits.

At 30 June 2009, had the market prices of the Company's investments increased by 5% net profit would have increased by $9.7 million (2008: $10.7 million). A 5% decline in market prices would have an equal and opposite impact.

Currency Risk
The Company has exposure to foreign currency denominated monetary assets and liabilities (cash and borrowings). Consequently, the Company is exposed to risks that the exchange rate of the Australian dollar relative to foreign currencies may change in a manner that has an adverse effect on the value of that portion of the Company's monetary assets or liabilities denominated in foreign currencies.

The Company held monetary assets and liabilities denominated in foreign currency at 30 June 2009. The Australian dollar equivalent of the foreign currency monetary assets and liabilities is detailed in note 7(b). Had the Australian dollar strengthened against each of these currencies, and with all other variables held constant, the impact on net profit would have been as follows:

30 June 2009			30 June 2008		
Australian dollar strengthens against:	by	Net increase in net profit	Australian dollar strengthens against	by	Net increase in net profit
		A$m			A$m
US Dollar	5%	(0.1)	US Dollar	5%	0.4
British Pound	5%	0.4	Bristish Pound	5%	0.3
Swiss Franc	5%	0.0	Swiss Franc	5%	0.0
Euro	5%	0.3	Euro	5%	1.0
		0.6			**1.7**

A decline in the Australian dollar against the foreign currencies would have an equal and opposite impact on net profit.

In addition to holding monetary assets and liabilities denominated in foreign currencies the Company holds other assets and liabilities denominated in foreign currencies and invests in listed international and Australian companies. Consequently, the Company is exposed to risks that the exchange rate of its currency relative to other foreign currencies may change in a manner that has an adverse affect on the value of that portion of the Company's total assets or liabilities denominated in currencies other than Australian Dollar.

At 30 June 2009, had the Australian dollar strengthened by 5% against its foreign currency exposure with all other variables held constant, net profit would have decreased by $9.7 million (2008: $8.6 million). A 5% decline in the Australian dollar would have an equal and opposite impact.

10. RISK MANAGEMENT (CONTINUED)

Currency Risk (continued)
The Company's total net exposure to fluctuations in foreign currency exchange rates at the Balance Sheet date is as follows:

	30 June 2009	30 June 2008
All amounts stated in AUD equivalents	$ '000	$ '000
Assets at fair value		
US Dollars	223,579	226,824
Euros	8,809	25,257
British Pounds	9,254	8,487
Swiss Francs	34,373	34,779
	276,015	295,347
Liabilities at fair value		
US Dollars [1]	(1,940)	12,017
Euros	8,298	27,875
British Pounds	10,088	9,200
Swiss Francs	1,013	-
	17,459	49,092

[1] Foreign currency cash balances held with Merrill Lynch are netted against foreign currency borrowings (refer note 7(b))

	30 June 2009	30 June 2008
Reconciliation of assets and liabilities exposed to f oreign currencies to the Balance Sheet:		
Assets - exposed to foreign currencies	276,015	295,347
Assets - not exposed to foreign currencies	44,812	49,209
Assets - as per Balance Sheet	320,827	344,556
Liabilities - exposed to foreign currencies	17,459	49,092
Liabilities - not exposed to foreign currencies	30,418	1,025
Liabilities - as per Balance Sheet	47,877	50,117
Net assets - exposed to foreign currencies	258,556	246,255
Net assets - not exposed to foreign currencies	14,394	48,184
Net assets - as per Balance Sheet	272,950	294,439

Interest Rate Risk
Interest rate risk is the possibility that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market interest rates. As at 30 June 2009 the Company had cash and borrowings and was subject to annual (365 day) interest rates as follows:

	Interest rate Cash / (Borrowings)	30 June 2009	Interest rate Cash/ (Borrowings)	30 June 2008
	%	$ '000	%	$ '000
Australian Dollars	3.00	54	7.25	112
Australian Dollars	(3.70)	(29,585)	(7.70)	(135)
US Dollars	0.29	1,940	(2.96)	(12,017)
British Pounds	(1.30)	(10,088)	(5.68)	(9,200)
Swiss Francs	(0.83)	(1,013)	-	-
Euros	(1.20)	(8,298)	(4.65)	(27,875)
		(46,990)		(49,115)

10. RISK MANAGEMENT (CONTINUED)

Interest Rate Risk (continued)
As at 30 June 2009, had interest rates increased by 100 basis points on floating rate cash and borrowings with all other variables held constant, the interest expense calculated on the balances held would increase by \$0.5m (2008: interest income would have increased by \$0.5m). A 100 basis point decline in interest rates would have an equal and opposite impact.

(b) Liquidity Risk

Liquidity risk is the risk that the Company will encounter difficulty in meeting obligations associated with financial liabilities.

This includes the risk that the Company:

(i) will not have sufficient funds to settle a transaction on the due date; and
(ii) will be forced to sell financial assets at a value which is less than they are worth.

As at 30 June 2009, borrowings repayable on demand total \$47.0m (2008: \$49.2m), amounts payable within 28 days relating to other payables is \$0.8m (2008: \$0.9m).

The Company has sufficient funds to meet these liabilities as and when due as all of the entities that the Company has invested in are highly liquid and are listed on major securities exchanges. As at 30 June 2009 the market value of the Company's investments is \$277.3m (2008: \$306.8m) and the value of these investments far exceeds the liabilities of the Company.

(c) Credit Risk

Credit risk represents the loss that would be recognised if counterparties failed to perform as contracted. Market prices generally incorporate credit assessments into valuations and risk of loss is implicitly provided for in the carrying value of on-balance sheet financial assets and liabilities as they are marked to market. The total credit risk for on-balance sheet items including securities is therefore limited to the amount carried on the Balance Sheet.

The Company minimises concentrations of credit risk by undertaking transactions with counterparties that are recognised and reputable or are recognised and reputable financial intermediaries with acceptable credit ratings determined by a recognised rating agency.

The Company has entered into an International Prime Brokerage Agreement (IPBA) with Merrill Lynch International (Australia) Limited (Merrill Lynch), a wholly owned subsidiary of Bank of America. The services provided by Merrill Lynch include lending, clearance, settlement and custody services. The IPBA with Merrill Lynch is in a form that is typical of prime brokerage arrangements. All of the Company's investments are held directly by Merrill Lynch International Bank (MLIB), as custodian.

During the financial year Merrill Lynch was acquired by Bank of America, one of the 'systemically important' global financial institutions.

The credit quality of Bank of America / Merrill Lynch's senior debt is rated, as at 30 June 2009, by Standard & Poor's as being A, and by Moody's as being A2. In the unlikely event of Merrill Lynch becoming insolvent the Company may rank as an unsecured creditor in regard to any investments that have been lent or used as collateral by Merrill Lynch.

(d) Fair Value Estimation
Refer to Note 1 (c) Investments at Market Value

11. INVESTMENT MANAGER

The Company has entered into an Investment Management Agreement with the Investment Manager, Magellan Asset Management Limited.

Base fee
The Investment Manager is entitled to a quarterly fee calculated as 0.3125% (excluding GST) of the market value of all assets less total indebtedness of the Company. The Investment Manager has excluded deferred tax assets from the calculation of the base fee thereby reducing the base fee amount.

Performance fee
The Investment Manager is entitled to an annual fee calculated as 10% (excluding GST) of the amount by which the absolute dollar value of the investment performance (after deducting the base fee) exceeds the Australian Dollar MSCI for the annual period, provided that:

(a) The total annual return in the relevant annual period exceeds the Australian Government 10- year bond rate (measured as an average of the 10-year bond rate published in the Australian Financial Review or similar publication) on the first day of each quarter occurring within the relevant annual period; and

(b) The portfolio value less borrowings on the last day of the relevant annual period is more than that on the last day of the last annual period for which a performance fee was paid to the Investment Manager within the last three years. The Investment Manager has also proposed and the Company has agreed that no performance fees will become payable until after the Company's Portfolio Value exceeds the initial Portfolio Value after the IPO.

The following amounts were incurred during the year:

	30 June 2009	30 June 2008
	$'000	$'000
Base fee	3,226	3,932
Performance fee	-	-
	3,226	3,932

12. CONTINGENT ASSETS, LIABILITIES AND COMMITMENTS FOR EXPENDITURE

No contingent assets or liabilities exist at balance sheet date.

The Company has no commitments for uncalled share capital on investments.

13. SEGMENT INFORMATION

Whilst the Company operates from Australia only (the geographical segment), it has global investment exposures due to its investments in many truly multinational entities and specific exposure to some countries from investments in other entities that generate revenues and operate predominantly within those countries.

The geographical locations are determined by the nature of the investment entity's business:

- International Companies are defined by the Company as being entities that generate 50% or more of their revenue and / or have operations in 15 or more countries outside of the country of domicile of their primary securities exchange.

- Entities that do not meet the Company's definition of International Companies are categorised by the country or region from which they predominantly operate in and derive their revenue from.

Note 3 provides further domicile information.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 30 JUNE 2009

14. BORROWINGS

During the year ended 30 June 2009 the Company continued to be provided with a borrowing facility by Merrill Lynch, a wholly owned subsidiary of Bank of America. The facility is associated with the International Prime Brokerage Agreements (IPBA) entered into by the Company and Merrill Lynch. The Company has granted Merrill Lynch a fixed charge over the Company's right, title and interest in the assets held in custody with Merrill Lynch, as security for the performance of its obligations under the IPBA. The credit quality of Bank of America /Merrill Lynch's senior debt is rated by Standard & Poor's as being A and by Moody's as being A2.

As at 30 June 2009 the borrowing facility, repayable on demand, was $47.0 million (30 June 2008: $49.2 million). In the unlikely event that Merrill Lynch required repayment upon short notice, the Directors are confident that the borrowings could be refinanced via an alternative lender or the borrowings could be repaid via settlement proceeds from the sale of part of the Company's investment portfolio, having regard to the high quality and liquidity of the Company's investments.

Under the Company's borrowing policy, total borrowings by the Company on the date of any drawdown on this facility must not exceed 20% of the Company's investments at market value. Merrill Lynch may to lend up to a multiple well above the Company's own borrowing limits, having regard to the high quality and liquidity of the Company's investments.

15. EVENTS SUBSEQUENT TO REPORTING DATE

On 30 July 2009 the Company purchased 7,573,149 shares for consideration of $4.5 million, completing the on-market buy-back of 20 million shares reducing shares on issue to 358,000,005.

On 26 August 2009 the Directors authorised a further buy-back programme of up to 20 million shares.

No other significant events have occurred since the end of the reporting year which would impact the Balance Sheet of the Company as at 30 June 2009 and the results for the year ended on that date.

16. RELATED PARTY INFORMATION

Disclosure relating to the management fees paid and payable to Magellan Asset Management Limited, a related party are set out in Note 11.

17. THE COMPANY

Magellan Flagship Fund Limited is a company limited by shares, incorporated and domiciled in New South Wales. Its current registered office and principal place of business is:

Level 7, 1 Castlereagh Street
Sydney NSW 2000

A description of the nature of the Company's operations and its principal activities is included in the review of operations and activities in the Directors' Report.

DIRECTORS' DECLARATION

FOR THE YEAR ENDED 30 JUNE 2009

In accordance with a resolution of the directors of Magellan Flagship Fund Limited, I state that:

1. In the opinion of the directors:

   (a) the financial statements, notes and the additional disclosures included in the Directors' Report designated as audited, of the Company are in accordance with the *Corporations Act 2001*, including:

   (i) giving a true and fair view of the financial position of the Company as at 30 June 2009 and of its performance for the year ended on that date.

   (ii) complying with Australian Accounting Standards and *Corporations Regulations 2001.*

   (b) there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.

2. This declaration has been made after receiving the declarations required to be made to the directors in accordance with section 295A of the *Corporations Act 2001* for the financial year ended 30 June 2009.

On behalf of the Board

Richard Warburton AO (Chairman)
Magellan Flagship Fund Limited
Sydney
26 August 2009

INDEPENDENT AUDITOR'S REPORT

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Independent auditor's report to the members of Magellan Flagship Fund Limited

Report on the Financial Report

We have audited the accompanying financial report of Magellan Flagship Fund Limited, which comprises the balance sheet as at 30 June 2009, and the income statement, statement of changes in equity and cash flow statement for the year ended on that date, a summary of significant accounting policies, other explanatory notes and the directors' declaration.

Directors' Responsibility for the Financial Report

The directors of the company are responsible for the preparation and fair presentation of the financial report in accordance with the Australian Accounting Standards (including the Australian Accounting Interpretations) and the *Corporations Act 2001*. This responsibility includes establishing and maintaining internal controls relevant to the preparation and fair presentation of the financial report that is free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances. In Note 1a, the directors also state that the financial report, comprising the financial statements and notes, complies with International Financial Reporting Standards as issued by the International Accounting Standards Board.

Auditor's Responsibility

Our responsibility is to express an opinion on the financial report based on our audit. We conducted our audit in accordance with Australian Auditing Standards. These Auditing Standards require that we comply with relevant ethical requirements relating to audit engagements and plan and perform the audit to obtain reasonable assurance whether the financial report is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial report. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the financial report, whether due to fraud or error. In making those risk assessments, we consider internal controls relevant to the entity's preparation and fair presentation of the financial report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal controls. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Independence

In conducting our audit we have met the independence requirements of the *Corporations Act 2001*. We have given to the directors of the company a written Auditor's Independence Declaration, a copy of which is attached to the directors' report.

Auditor's Opinion

In our opinion:

1. the financial report of Magellan Flagship Fund Limited is in accordance with the *Corporations Act 2001*, including:
   - (i) giving a true and fair view of the financial position of Magellan Flagship Fund Limited at 30 June 2009 and of its performance for the year ended on that date; and
   - (ii) complying with Australian Accounting Standards (including the Australian Accounting Interpretations) and the *Corporations Regulations 2001*.
2. the financial report also complies with International Financial Reporting Standards as issued by the International Accounting Standards Board.

Report on the Remuneration Report

We have audited the Remuneration Report included in pages 15 to 17 of the directors' report for the year ended 30 June 2009. The directors of the company are responsible for the preparation and presentation of the Remuneration Report in accordance with section 300A of the *Corporations Act 2001*. Our responsibility is to express an opinion on the Remuneration Report, based on our audit conducted in accordance with Australian Auditing Standards.

Auditor's Opinion

In our opinion the Remuneration Report of Magellan Flagship Fund Limited for the year ended 30 June 2009, complies with section 300A of the *Corporations Act 2001*.

Ernst & Young

Ernst & Young

R Da Silva

Rita Da Silva
Partner
Sydney
26 August 2009

SHAREHOLDER INFORMATION

DISTRIBUTION OF SHAREHOLDERS

The distribution of shareholders of the Company as at 20 August 2009 is presented below:

Distribution Schedule of Holdings	Holders	Number of Ordinary Shares	Percentage of Shares in Issue
1-1,000	95	72,177	0.020
1,001-5,000	402	1,357,066	0.379
5,001-10,000	995	8,725,973	2.437
10,001-100,000	2,773	100,962,278	28.202
100,001 and over	372	246,882,511	68.962
Total	**4,637**	**358,000,005**	**100.000**
Number of holders with less than a marketable parcel	45	22,630	0.006

TWENTY LARGEST SHAREHOLDERS

The names of the twenty largest shareholders of the Company as at 20 August 2009 are listed below:

Holder Name	Number of Ordinary Shares	Percentage of Shares in Issue
Magellan Financial Group Limited	44,727,166	12.49
UBS Wealth Management Australia Nominees Pty Ltd	17,479,745	4.88
Cogent Nominees Pty Limited	15,647,686	4.37
Forbar Custodians Limited	10,925,800	3.05
Mr Christopher Mackay	10,450,506	2.92
Cairnton Holdings Limited	10,000,000	2.79
Naumov Pty Ltd	7,658,293	2.14
Mr David Dixon	3,748,392	1.05
Perpetual Trustees Consolidated Limited	3,432,600	0.96
J P Morgan Nominees Australia Limited	3,076,626	0.86
National Nominees Limited	2,184,779	0.61
Falcon Nominees Investments Pty Ltd	2,000,000	0.56
Wulura Investments Pty Ltd	2,000,000	0.56
HSBC Custody Nominees (Australia) Limited	1,932,900	0.54
Citicorp Nominees Pty Limited	1,926,033	0.54
Pokana Pty Ltd	1,844,000	0.52
Investment Custodial Services Limited	1,691,500	0.47
ANZ Nominees Limited	1,570,200	0.44
UBS Nominees Pty Ltd	1,301,017	0.36
Bond Street Custodians Limited	1,300,000	0.36
Total shares held by the twenty largest shareholders	144,897,243	40.47
Total shares in issue	**358,000,005**	**100.00**

SUBSTANTIAL SHAREHOLDERS

The name of the substantial shareholders of the Company and their holdings as at 20 August 2009 are listed below:

Shareholder	Number of Ordinary Shares	Percentage of Shares in Issue
Magellan Financial Group Limited	44,727,166	12.49
Christopher Mackay and Associates	18,914,299	5.28

Ordinary Share Capital

All issued ordinary shares carry one vote per share and carry the rights to dividends.

CORPORATE DIRECTORY

Directors
Richard Warburton AO
John Ballard
Andy Hogendijk
Chris Mackay
Hamish Douglass

Company Secretaries
David Simpson
Leo Quintana

Registered Office
Level 7, 1 Castlereagh Street
Sydney NSW 2000
Telephone: +61 2 8114 1888
Email: info@magellangroup.com.au
Fax: +61 2 8114 1800

Investment Manager
Magellan Asset Management Limited
Level 7, 1 Castlereagh Street
Sydney NSW 2000
Telephone: +61 2 8114 1888
Email: info@magellangroup.com.au
Fax: +61 2 8114 1800

Auditors
Ernst & Young
680 George Street
Sydney NSW 2000

Share Registrar
Registries Limited
Level 7, 207 Kent Street
Sydney NSW 2000
Telephone: +61 2 9290 9600
Fax: +61 2 9279 0664
Email: registries@registries.com.au

Securities Exchange Listing
Australian Securities Exchange
ASX code: MFF

Website
http://www.magellangroup.com.au/MFF

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MFG MAGELLAN
FLAGSHIP FUND LIMITED