Chairman's Address

To the 3rd Annual General Meeting

Tuesday 20, October 2009

Introduction

I plan to outline the Company's financial performance for the year to June 30 2009 and update you on the Company's subsequent progress and discuss the Company's outlook.

Your Directors continue to be satisfied with the Flagship Fund's very high quality portfolio. As you will hear shortly, the Company's investment performance for 2008/9 solidly exceeded market benchmarks and we have solid grounds for optimism

Financial Performance

The decline in the Company'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 the Company handled the extreme conditions of 2008/9 better than many. We are also confident about the business prospects for the high quality companies in our portfolio. We expect that our focused, disciplined investment approach will be rewarded with sustained positive performance, over time

The decline in the NTA equated to a loss after tax of 3.96 cents per share as the Company 'marks to market' all share price and foreign exchange market price movements for the year.

As all investors are aware, equity markets in 2008/9 were very difficult and volatility also continued in currency markets. We hope that you had the time to read the Financial accounts and Investment Manager's Report in the Annual Report and 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 uncertainty.

We continue to supply considerable detail on the Company's investments. These have been included in the Annual Report and other regular Reports. The Company also keeps shareholders abreast of portfolio composition and market trends through the monthly NTA announcements which includes commentary.

MFF'S Portfolio

During the first three quarters of 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 for much of the year at levels below those prevailing a decade ago.

In this environment, our portfolio was further upgraded with purchases of select companies with global leading businesses. More significant portfolio acquisitions during the year included shares in Nestle, YUM! Brands, Wal-Mart, Google, Coca-Cola, Proctor & 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.

Whilst our portfolio companies have excellent business resilience, they are not entirely insulated from the chill winds of the recession. Near term economic conditions are difficult in much of the world. However we expect that our portfolio companies will likely be disproportionate beneficiaries of the 1 billion or so newly middle class, newly urbanised consumers expected over the coming decades in emerging markets as well as retaining leadership in more established markets. Many of our portfolio companies combine excellent cash flows with above average growth potential.

The Company continues to provide valuable diversification for Australian and New Zealand investors in terms of companies, currencies and business geographies. We are pleased that The Company maintained its investment discipline and, particularly, that we continued to buy shares in quality businesses during the panic and widespread falling prices in 2008/9.

On Market buy-back and dividends

In July, 2009 the Company completed its on-market share buy-back of 20 million shares at an average price of approximately 56 cents per share, which represents a 22% discount to MFF's average net assets per share during the buy-back period. We recently announced that the Company will undertake a further on-market share buy-back of up to an additional 20 million shares over the next 12 months and as at 16 October 2009, another 1.2 million shares had been bought back. Shares bought back will subsequently be cancelled. The Company'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 the Company's Balance Sheet strength after the shares are bought back

Your Directors have also discussed the outlook for dividends from the Company and will look seriously at introducing a dividend provided the Company achieves accounting profitability.

Outlook

Last year at the AGM I said that "your Directors consider that MFF shareholders have grounds for optimism notwithstanding our cautious view of the near term economic outlook." We continue to hold that view and believe that a number of our portfolio companies are making very solid progress in their markets. We expect that the Company will benefit materially over time from the growing Cashflows generated by our focussed portfolio of global leaders. We also continue to believe that it is an appropriate time for investors to focus resiliently on the highest quality companies. Investment performance remains the absolute key factor for the Company. Exchange rates are also extremely important at the moment, as shown by the adverse impact on MFF's Australian Dollar values from the 50% rise in the value of the Australian Dollar since March. I now invite Chris Mackay to make some remarks about the Flagship Fund's portfolio investment approach, the outlook for the portfolio and exchange rates.

Richard Warburton AO

Chairman

Comments by Chris Mackay, Chief Investment Officer

Thank you Chairman. Today I will seek to deal with 4 of the most important issues in assessing an investment in MFF. Number 1 is the Portfolio, the most important issue and the issue on which I will finish. This is overwhelmingly a positive story with a lot of future potential. Number 2 is how did we react under the extreme pressure of disintegrating financial markets and economic problems during last year, and what does that tell shareholders about how we will act in the future? Number 3 is foreign exchange movements which are currently a major headwind for the market value of the portfolio and for the market price of MFF's shares. Number 4 is capital management and this includes share buybacks, our strong balance sheet, future dividends and our scope to make purchases that increase the underlying value of MFF shares.

There are of course many other issues on which shareholders might have questions …for example Hamish Douglass has previously provided great insight in relation to the financial crisis, and we would be very happy to answer questions later in the meeting.

Capital Management

The first aspect of capital management is the Balance Sheet and I will deal in turn with our assets and then liabilities.

MFF is a relatively simple and, we hope, transparent investment story. We have a strong core, being our most significant investments which comprise 15 - 20 companies which are of the highest quality and combine well below average business risk with above average future potential. Our investments are heavily concentrated in companies that are the lowest cost producers, have the strongest brand names, have #1 or #2 market shares, have pricing power in times of inflation or deflation, are geographically diverse with leadership in many markets around the globe and, as a result, generate billions of dollars every year in free cashflow (that is, cash that is earned by the business after subtracting those amounts which have to be reinvested back into inventory or new plant and equipment, marketing, research and development). These companies have strong bases, [they are] multi legged stools that can cope with recessions or worse in much of the world whilst achieving very satisfactory risk adjusted business returns. In many cases it is almost inevitable that the companies will materially increase their future revenues, profits and cashflows over many years without taking significant business risks. There are very few companies in the world in which investors can have the same confidence.

The shares in these companies are traded on stock exchanges around the world in high volumes with daily buying and selling levels which are many multiples of our total holdings. Hence our portfolio combines relatively high business stability (particularly when considered with an appropriate focus on duration) with very high liquidity.

MFF is also a closed end company; in other words when investors panic, MFF is not vulnerable to a ‘run’ which requires assets to be sold. This combination means that it is not inappropriate to introduce a limited amount of gearing into the capital structure and we have done this with the 20% borrowing limitation. At the moment borrowing costs are artificially low and they range from below 1% to about 4% annual costs depending on the currency. At this time, the limited borrowings by MFF to buy quality is a sensible utilisation of the capital structure. As markets continue to ‘normalise’, investors should expect borrowings to be repaid and gearing eliminated during a full cycle.

As mentioned by the Chairman, MFF has now bought back approximately 21.2 million shares since starting the buyback last year. We believe that selling shareholders benefitted because additional market liquidity has been provided by the buyback. Shareholders who continue to hold may benefit if the prices paid are below the underlying or intrinsic value of the MFF shares. The price has been below the prevailing market prices for the portfolio, as shown by the NTA figures released to the ASX weekly. The benefits to NTA so far are moderate but cumulative and the buyback to date has added about $3 million or slightly less than 1 cent per share to pre tax NTA.

The Chairman also mentioned that Directors will examine carefully whether to introduce a dividend provided there are accounting profits. We intend to seek to continue the buyback and examine dividends provided there are accounting profits.

The choices for MFF are not equivalent to Nestlé and Procter & Gamble which have multi billion dollar annual cash inflows and thus they are able to conduct $25 billion buybacks and increase dividends as well as spending billions of dollars on expanding their market and product penetration.

In order to keep MFF's borrowings below the 20% limit which we regard as both sensible and appropriate, MFF can fund new share purchases, buybacks and dividends only from dividends received and from the sale of existing shares in the portfolio. Hence there are very obvious and immediate opportunity costs for MFF in these decisions. For much of MFF's history, the share prices for almost all of the companies in which we are most interested have been well below levels we regard as reflecting their potential…at the start there was a flood of money into emerging markets, structured finance, alternative investments and commodity funds amongst others…this was followed by the rolling series of panics and economic crises where almost every asset class was sold off dramatically and the previously 'hot' investments hit hardest or in some cases forced into bankruptcy…the latest phase has seen a recovery in markets with many of the strongest market recoveries being in the most risky investments whilst the share prices of many of the most solid companies, such as McDonald's, Wal-Mart and Nestle, have not risen as far from the March lows and continue to offer very significant value in our view.

This situation is not permanent…ultimately investments reflect the free cashflow generated by them and our companies are world leading free cashflow generators, whatever measurement basis is used. One of the leading Professors of Value Investing recently described the phenomenon of the current "Dash to Trash" as "People love lottery tickets" and hence they buy poorer quality investments as they get popular and overpriced, and inevitably underperform in aggregate over time, after rewarding some winners and holding hope for many. A reversion to Quality is inevitable and we are confident that one day a number of the companies in our portfolio will actually become overpriced when many investors decide that Quality is again the way to invest, particularly in emerging markets, and there are fewer clouds on the economic horizons for more developed markets.

As it is highly probable that our quality companies will perform well over time, we are comfortable deploying capital buying that portfolio via the buyback and thereby seeking to add incremental value.

We do continue to assess the mix of the portfolio and to assess opportunities where prices have fallen on their own and in comparison with the buyback; for example we added when Kraft's share price fell after it announced that it was considering a takeover offer for Cadbury and we sold others where risk/reward in the context of our portfolio became more evenly balanced. Less common for MFF has been where prices went beyond our risk adjusted view on value (as happened briefly for Wells Fargo, MasterCard and Google) where we sold and subsequently repurchased. These portfolio rebalance situations will continue to be a primary source of capital for the ongoing buyback and purchases of securities.

The buyback may also provide confidence for some investors in MFF who have more of a trading mentality, as they see from our actions that MFF has been a buyer in volume of its own stock under the buyback and shareholders will have particularly noted that we were a significant buyer during the recent very panicked market episodes.

Thus, a key message for shareholders today is that we will continue be very active in seeking to use our available capital to boost MFF's underlying asset value and to give investors confidence so that in time the share price properly reflects the underlying values.

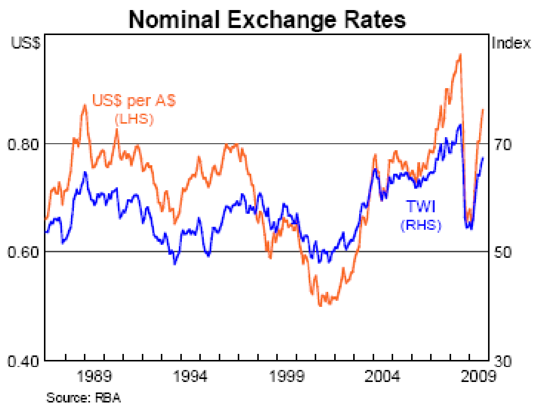
Foreign Exchange Movements

As you are aware, MFF has had an unhedged currency position since inception. This helped reduce some of the extreme equity market price volatility in the period to March when reported back into Australian dollars, but has been a drag on recent performance as the Australian Dollar has strengthened by about 50% since its March lows. In the period from July 1 to September 30 this year, the pre tax NTA rose approximately 6 cents and this comprised a 13 cent increase in equity values offset by a 7 cent negative currency impact. The currency volatility continues to disguise the ongoing positive market prices of the portfolio in comparison with global indices measured in constant currency terms with outperformance of about 2.5 and 5 percentage points over the latest 3 and 6 months (respectively) to 30 September, although those figures trail the stronger rebound in the Australian stock market.

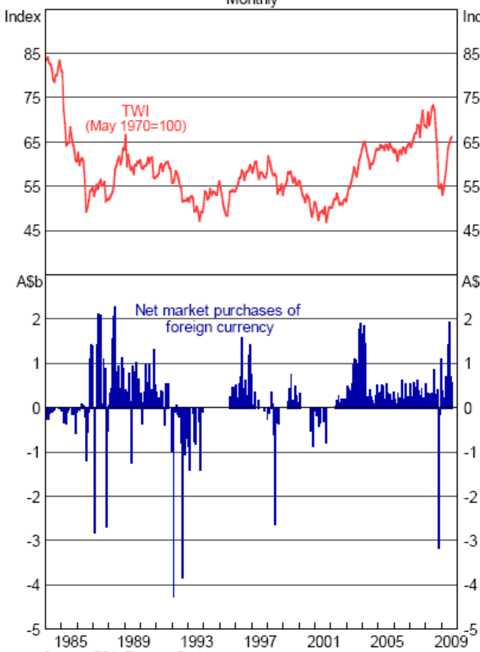
During the first four months of this year we closely examined whether to hedge a substantial portion of the portfolio. The decision not to proceed was wrong, as markets rebounded far more dramatically than I anticipated. We were concerned about the risks of the economic crisis worsening materially and Australia suffering a proportionately worse impact and hence the risks that the currency potentially retested the types of levels seen during the Asian crisis. We were also conscious of the correlation between the Australian dollar and equity markets and that an unhedged currency position worked as a partial hedge against market and economic deterioration. By the time it was clearer that the near term economic outlook was less clouded and markets were to benefit from the unprecedented fiscal and monetary stimulus, the Australian dollar had already appreciated well off its lows. The context of the portfolio is relevant, as the best decision we made at the time was to move to a fully invested position in the face of market panic and widespread selling…we clearly were right to be buying shares in quality companies at very significant discounts to our assessment of fair values and many have increased in market price despite the “Dash to trash” mentioned earlier.

MFF now faces a situation where the Australian dollar has appreciated dramatically and many commentators expect it to rise further in the short term. We will not now go and hedge the portfolio’s currency at the levels currently prevailing…the time to consider that carefully was at the start of the year, not when the currency is strongly in favour and well above Purchasing Power Parity and longer term trading levels. Individual shareholders, brokers and financial planners who have MFF as part of their portfolio on their client portfolios continue to assess whether to hedge their own exposures in the context of their portfolios.

We seek to look at fundamentals, both good and bad, in assessing and reassessing currency positions. We look carefully at the material the RBA releases from time to time and you will see a series of charts with which you can consider some of the local factors which will affect currencies over time. Australian shoppers recognise purchasing power parity benefits and that they can save thousands of dollars this holiday season by going online and visiting global sites with low prices and incredible ranges such as eBay’s merchants, and provided they have the protections of American Express’ Buyers Advantage or PayPal.

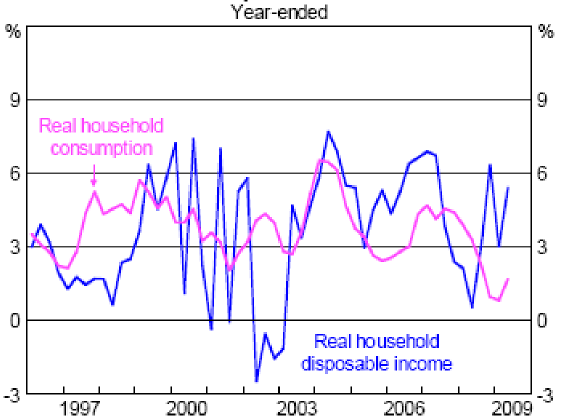


Australian Dollar and RBA Foreign Exchange Market Operations
Monthly



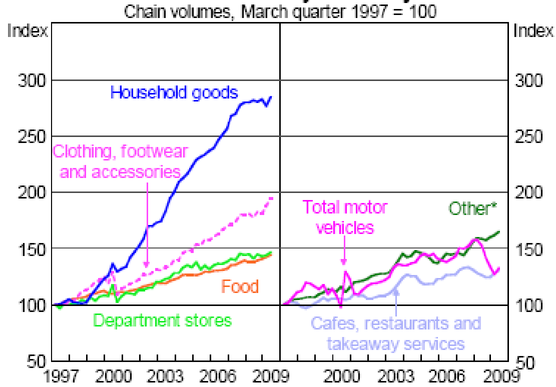
Sources: RBA; Thomson Reuters

Household Consumption and Income Growth
Year-ended



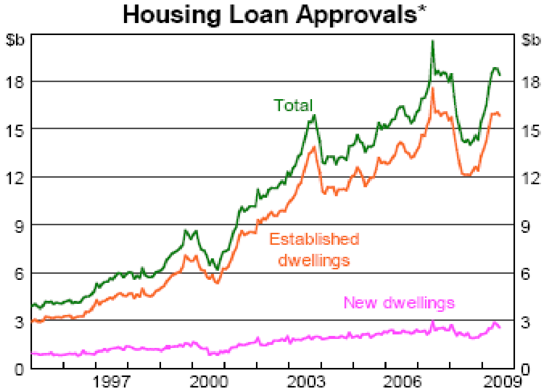
Sources: ABS; RBA

Retail Sales by Industry
Chain volumes, March quarter 1997 = 100



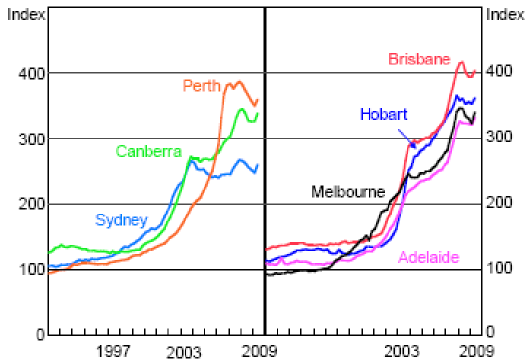
* Other includes several components, such as pharmaceuticals and second-hand goods
Sources: ABS retail trade survey and ABS sales of new motor vehicles

Housing Loan Approvals*

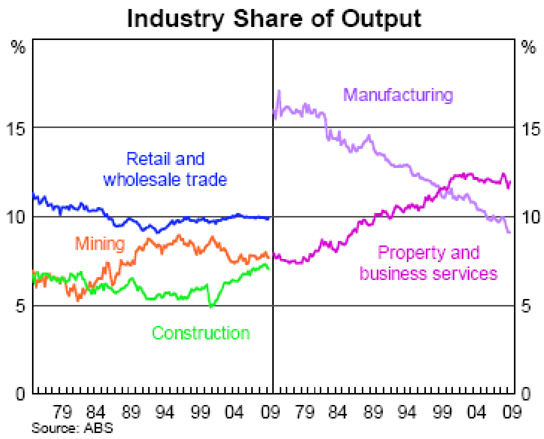


* Excludes refinancing; includes investors and owner-occupiers
Source: ABS

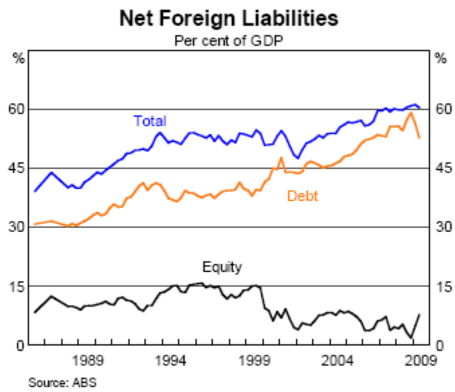
Established House Prices*
1989/90 = 100



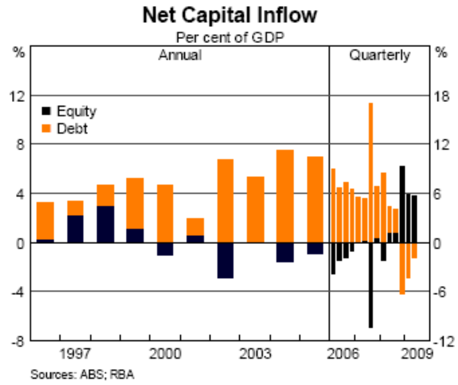
* Spliced series; settlement dated data prior to 2002
Source: ABS



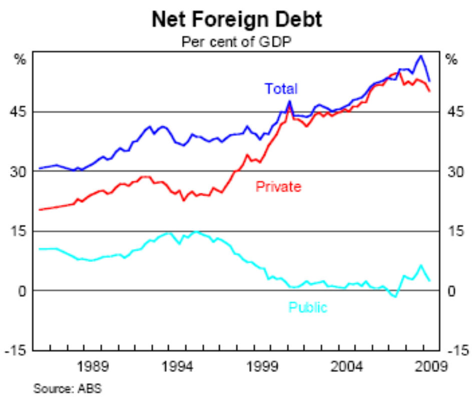
Industry Share of Output
%
Manufacturing
Retail and wholesale trade
Mining
Property and business services
Construction
15
10
5
0
79 84 89 94 99 04 09 79 84 89 94 99 04 09
Source: ABS



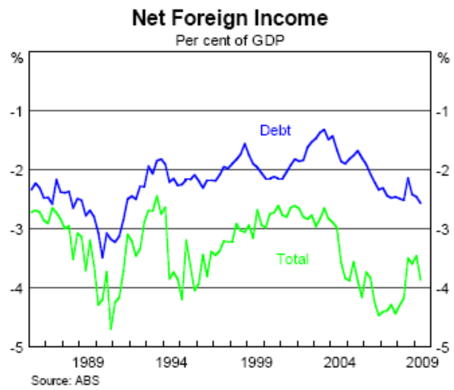
Net Foreign Liabilities
Per cent of GDP
%
Total
Debt
Equity
60
45
30
15
0
1989 1994 1999 2004 2009
Source: ABS



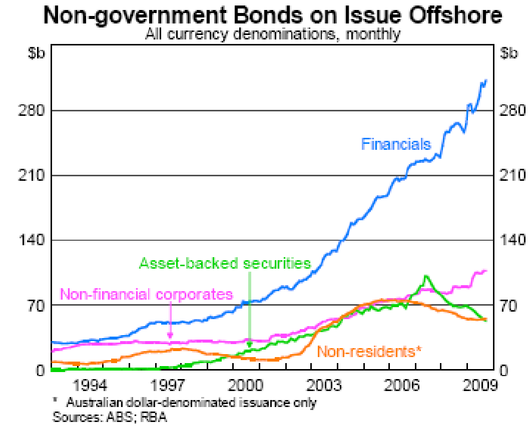
Net Capital Inflow
Per cent of GDP
Annual
Quarterly
%
Equity
Debt
12
8
4
0
-4
-8
18
12
6
0
-6
-12
1997 2000 2003 2006 2009
Sources: ABS; RBA

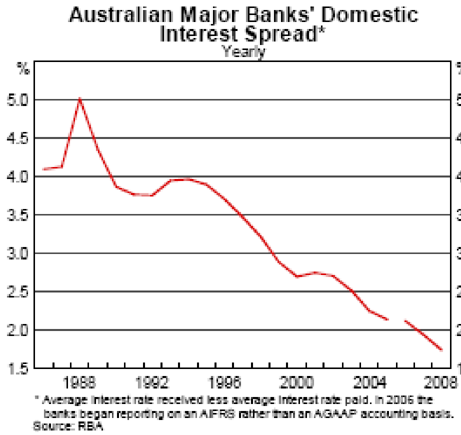


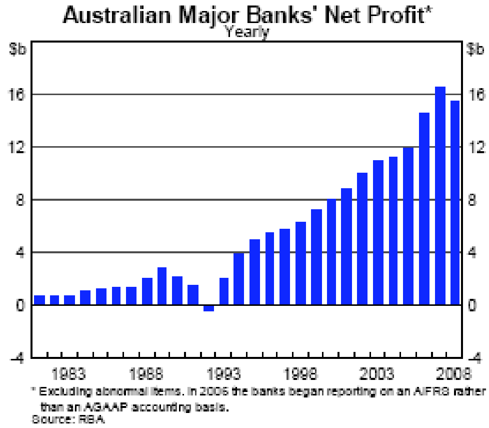
Net Foreign Debt
Per cent of GDP
%
Total
Private
Public
45
30
15
0
-15
1989 1994 1999 2004 2009
Source: ABS



Net Foreign Income
Per cent of GDP
%
Debt
Total
-1
-2
-3
-4
-5
1989 1994 1999 2004 2009
Source: ABS







If Australia was addressing the underlying fundamental imbalances in our economy and global positioning we would have had a different perspective on currency hedging. In my view Australia is likely to have the worst current account deficit of any major industrialised nation over the next few years, with the possible exception of Spain which has suffered a severe housing and unemployment crisis. Listen for the commentary if the Balance of Payments again reaches the 6% decried by Mr Keating as reflecting a Banana Republic 20 years ago, in this case despite unsustainably positive terms of trade. The economic crisis has increased Australia's dependence upon monetary flows but now the structural imbalance is worsened because global portfolio flows (debt and equity) are driven by short term focussed hedge funds, and the level of foreign direct equity investment has stepped up over recent years and this investment seeks equity returns. Not even the US crisis has degenerated into a [massive] foreign purchase of the country's means of production, as much of the US focus remains on the purchase of US Treasuries (i.e. Government Debt which yields 4% or so compared with the significantly higher equity returns US companies earn on their own offshore investments). The Crisis required the Australian Federal Government to guarantee of State Government and financial institutions' debt given the overreliance on offshore markets to fund recurrent expenditure and mortgage lending, and those markets effectively shutdown. The indebtedness of Australian consumers has not reduced materially and exceeds that of even the overleveraged UK and US consumers as a proportion of GDP. The economic impact has been put off because the vast majority of Australian mortgages and home equity loans are variably priced and the cuts in official interest rates were almost entirely passed on in lower variable rates. We expect that, in time, the Crisis will show that excessive borrowing for consumption and inexorable rises in Government costs and regulation are unsustainable, even for a country with Australia's resource advantages.

Currencies deal with relativities, and many of the policies of the US and UK authorities do not appeal to us and even Brazil has a Government Sector at about 50% of GDP. In contrast, a recent report said that Switzerland was continuing to achieve a balance of Payments surplus and would even achieve a budget surplus for 2010, as they did not engage in the stimulus spending of Governments elsewhere in the world. As discussed in the Investor Report, politicians will struggle with the choices needed to wind down the stimulus and the risks from the global imbalances have not been reduced by the stimulus. Whilst we accept the billions of dollars in aggregate increased profitability that has accrued to MFF's portfolio from the stimulus, the costs of the stimulus are still to be paid.

We expect that most investors have not considered that the Chinese currency is close to the world's worst performer despite strong Chinese economic growth. Other key exceptions to market forces include subsidies for oil and other energy use particularly in developing markets and official interest rates set by officials or committees. These distortions are a long way from having been worked through.

Our views regarding currency movements are summarised as follows:

- we are not hedging at these levels although we looked closely earlier in the year and will look again if the Australian dollar falls markedly.

- we are cautious about the long term impact of some government policies and we are looking closely at individual countries for positive policies which likely will benefit individual currencies over time, other things being equal.
- the Australian dollar is well above purchase price parity measures and its historical trading ranges. The flows into commodity investment funds and emerging markets are again at record levels and this increases demand for Australian Dollars and selling of US Dollars. Whilst this may persist for some time and could well go significantly higher, we expect it to correct in time. Whilst China's demand is important for Australian minerals, the resource sector is only about 8% of Australian GDP and even with a 50% rise it is important but not the sole determinant for the Australian economy or currency.
- whilst the currency impact has been disproportionately significant in the first few years for MFF, its importance diminishes over time via the operation of mathematics upon company performances. Thus, provided that we have selected the investments appropriately and not overpaid for them, MFF's value will increase over time even if contrary to our expectations the AUD continues to rise well above its historical trading ranges and never falls.
- MFF's portfolio comprises business operations in every country and currency in the world which provides some natural hedges.

Response to the Crisis

Even the most experienced market participants were tested in the markets which prevailed for the first three quarters of 2008/9. Many prices declined day after day and confidence in both markets and the real economy evaporated and markets declined again as deteriorating economic outlooks became reality.

In this context we tested and retested business cases and discarded some investments where prices approximated fair value (briefly in that period) or where business risks had risen. In some cases we sold simply to make room for purchase of companies of the quality of Google, Coca Cola and Colgate-Palmolive at exceptional prices.

We didn't "sell everything" and go to cash in anticipation of the crisis. We felt all the way along that values on offer were very attractive relative to the demonstrated earnings power and in many cases values were simply compelling. We also didn't buy the "cheapest" most beaten down stocks in the crisis…it would have been a mistake in our view to have bought the highly leveraged financials during the crisis and a number didn't survive, but now some that survived have been the strongest share price performers in the rebounding markets. We will attempt to stick to quality irrespective of other alternatives which we believe carry greater business risks.

When we established MFF, we foreshadowed aiming for about 85% being invested in core outstanding companies and we felt that we would need to invest about 15% or so in high quality but less outstanding companies, as the best companies would likely be fully priced from time to time. The Crisis gave us the opportunity to go to more than 95% invested in companies we regard as outstanding and also to limit the spread of companies. Thus we have a portfolio of about 30 companies with 15 or so larger positions forming the core. We expect to stick with this more focussed portfolio as we feel much more confident about this than having to make an assessment between two more lowly ranked or riskier companies.

Coming out of the Crisis, we will continue to be driven by business Quality and Value and seek to balance capital protection with our assessment of risk adjusted returns. We will continue to offer portfolio diversification in terms of companies, countries, currencies and our preferred focus industries. We are very cautious about many investments there is considerable oversupply in many industries, and we believe that much of the oversupply is structural (and hence will likely impact longer term ROEs).

Very few investors have a genuine multi year view on companies and hence we should have more patience and scope to stick with outstanding investments. For example Yum! Brands is regularly ranked as one of the top global companies investing in China, as well as its strong international business. It is far more probable than not that they will about double their number of restaurants globally over the next 15 years including at least a four fold increase in China. It is also probable that their excellent return metrics will be about maintained in part thanks to their franchise structure outside of China. However most analysts and institutional investors have to be concerned with anticipating the possible impact on the share price of the next quarterly earnings and monthly same store sales levels [as an aside, their latest quarter showed 19% diluted earnings per share growth despite consumer weakness in China]. Similarly, almost all investors would have a very positive view on the future potential of Google (which last quarter as a 10 year old company generated an amazing US$2.54 billion in free cashflow, has US$22 billion cash on balance sheet and is already the world's most profitable media company) and this includes those investors who sold to us in the March period at less than half of current prices and below 10x forward free cashflow.

MFF's Quality Portfolio

This slide is the most important by far in considering MFF's investment potential. An Australian investor cannot come close to replicating businesses of this quality in the local market.

Magellan's Quality Portfolio

World leading quality pricing power minimises the risk of permanent capital loss with attractive risk adjusted growth prospects (95% of MFF's portfolio value as at 30/9/09)

- Extremely high quality free cash flow generators with focussed exposure to growth as market leaders in the developing world

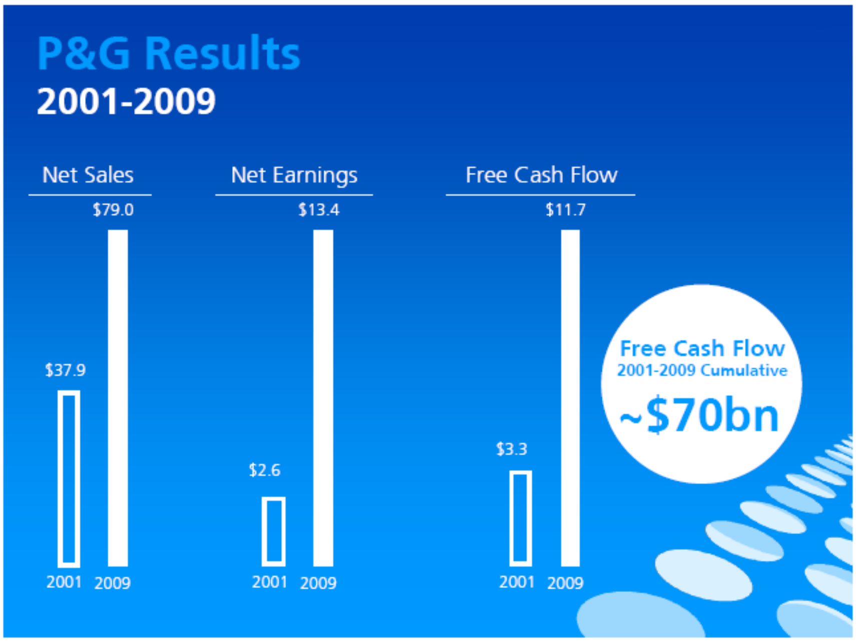
- Lowest cost, market leading non-discretionary retailers with increasing profitable exposures in emerging markets

- Businesses that exhibit powerful cash generative "network economics" in developed and emerging markets

[Sales of Microsoft and MasterCard since 30/9/09]

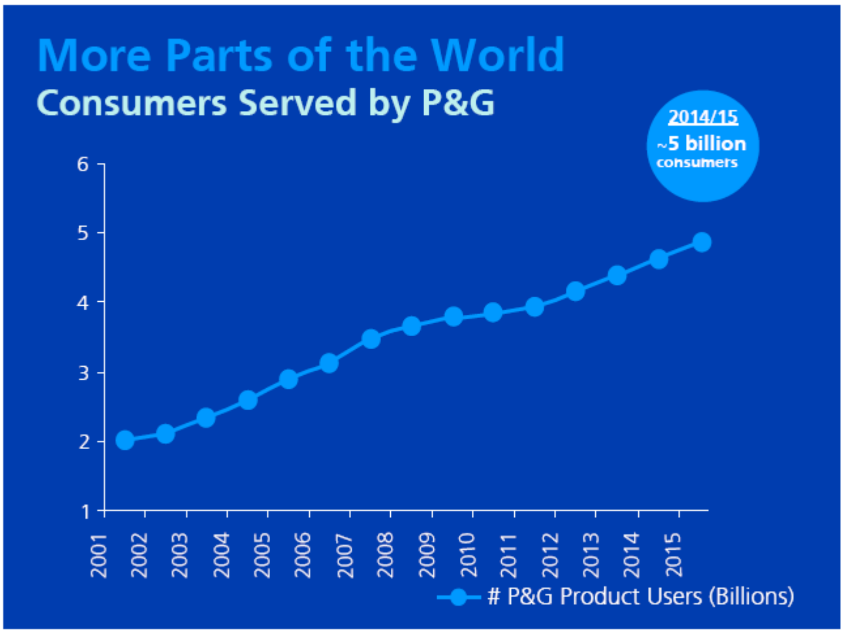
The following slides are from Procter & Gamble's Annual Meeting earlier this month and a recent presentation from the Pacific Group President for Coca-Cola. They illustrate the extraordinarily high Quality levels we are seeking, and we were fortunate to be able to buy both companies at attractive prices.

Case Studies: Procter & Gamble



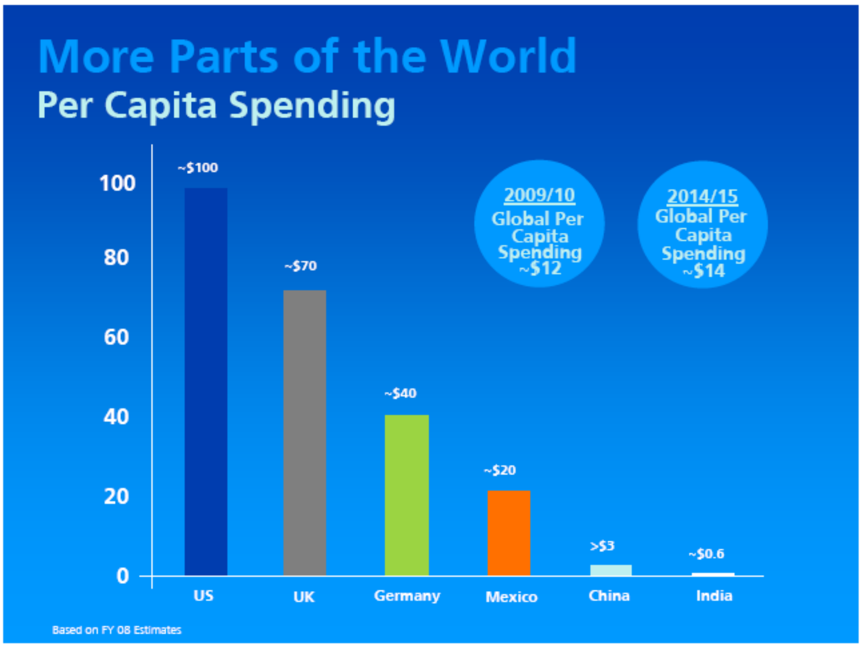
Procter & Gamble 2009 Annual Meeting of Shareholders

Case Studies: Procter & Gamble



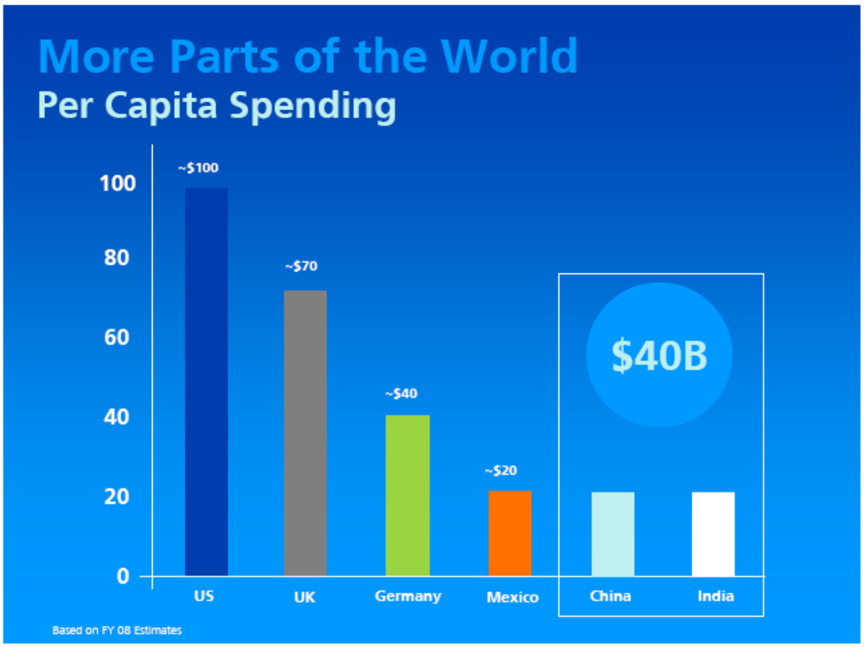
Procter & Gamble 2009 Annual Meeting of Shareholders

Case Studies: Procter & Gamble



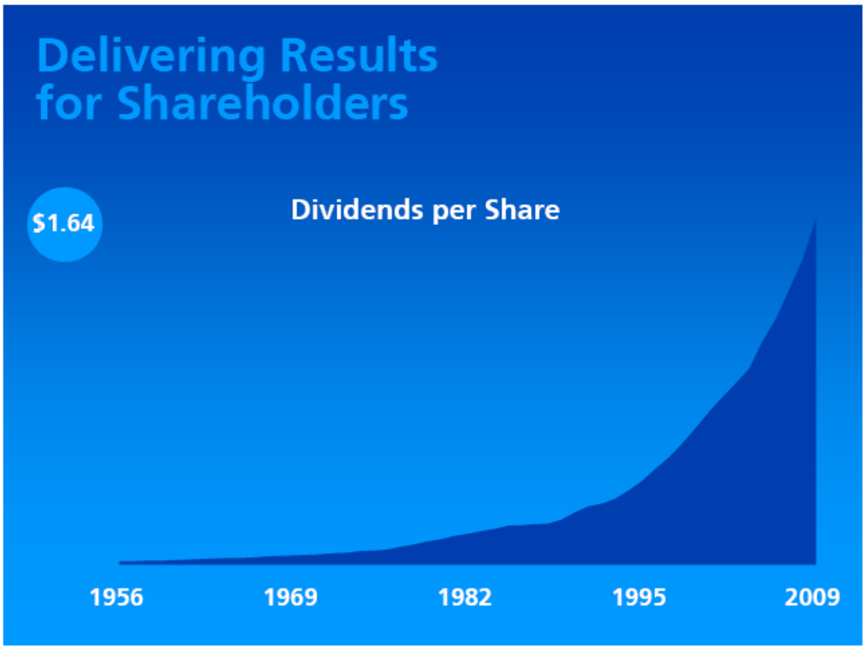
Procter & Gamble 2009 Annual Meeting of Shareholders

Case Studies: Procter & Gamble



Procter & Gamble 2009 Annual Meeting of Shareholders

Case Studies: Procter & Gamble

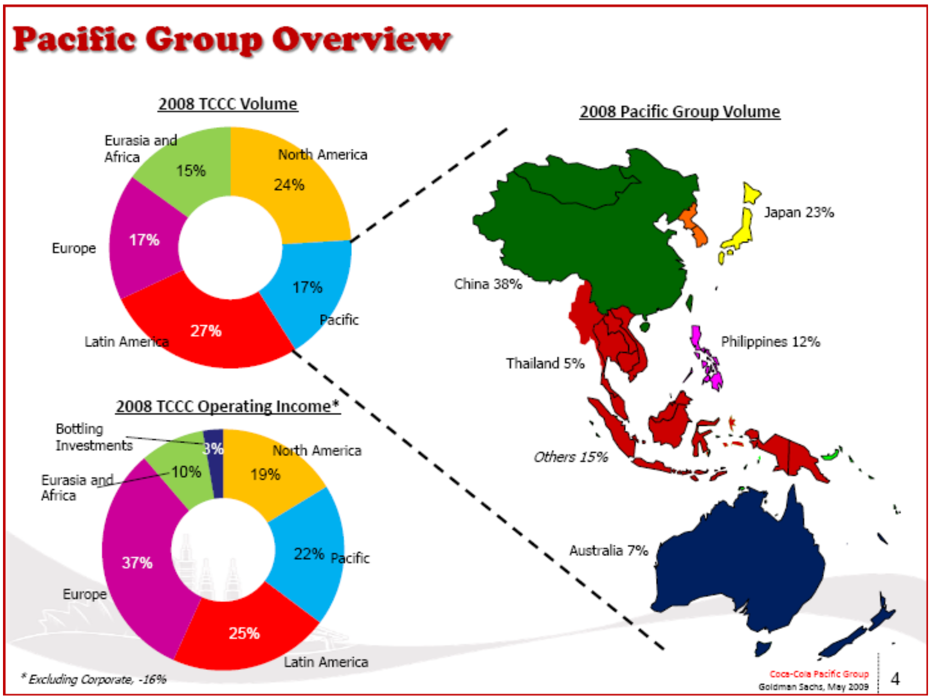


Procter & Gamble 2009 Annual Meeting of Shareholders

Case Studies: Coca-Cola Pacific

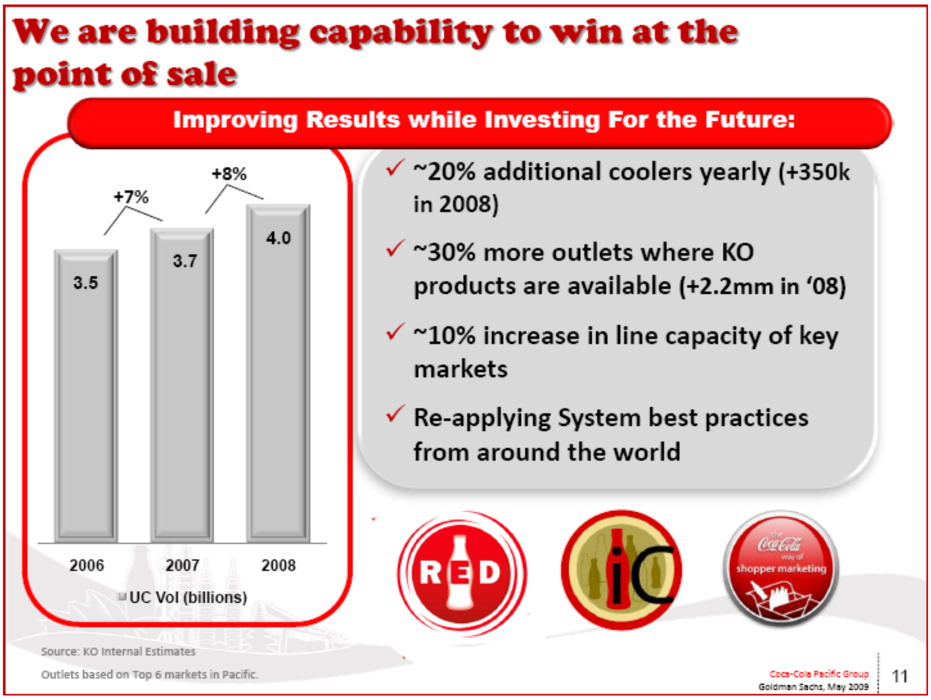
Coca-Cola: Goldman Sachs Consumer Products Symposium 2009 Conference, New York, 14 May 2009 – Glenn Jordan, Pacific Group President

Case Studies: Coca-Cola Pacific



Coca-Cola: Goldman Sachs Consumer Products Symposium 2009 Conference, New York, 14 May 2009 – Glenn Jordan, Pacific Group President

Case Studies: Coca-Cola Pacific



Coca-Cola: Goldman Sachs Consumer Products Symposium 2009 Conference, New York, 14 May 2009 – Glenn Jordan, Pacific Group President

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