

Small Cap Fund

Sharemarket Commentary

The Australian sharemarket rose 4.5% during July aided by a rally in the US after many US companies reported reasonable results. The US rally helped all world markets rally with European markets up 6% while Asian markets rose 5.4%. US company results showed very subdued revenue growth but were helped by continued tight cost control and reduced capital expenditure. This trend was reflected in US economic data released over the month which reflected a very soft economy particularly in the housing, manufacturing and services sectors.

The global stockmarket rally during July was characterised by fairly thin volumes as investor sentiment remained fickle. There was very limited news flow out of Australian companies with most companies due to update investors when reporting their full year results in August. Domestically, the RBA kept interest rates at 4.5% influenced by the release of the June quarter CPI which came in at 0.6%, well below expectations. The Australian economy continues to travel reasonably well as evidenced by an improvement in consumer confidence and solid employment growth. The Australian dollar rallied by 7% to 90.1 US cents over the month aided by firmer commodity prices while the yield on Australian 10 year government bonds rose 0.11% to 5.2%.

The rally in global markets and commodities, combined with the Commonwealth Government's watering down of their proposed RSPT, led to a rally in the more cyclical sectors in the mid and small-cap indices. The gains were led by the Materials and Energy sectors with the Industrials sector also recording strong gains on the back of a rally in several mining services companies.

It was another busy month for corporate activity with Graincorp and AWB announcing a nil premium scrip merger, the Canadian Pension Plan Investment Board submitting an indicative non-binding and conditional offer for Intoll of \$1.535 per share, while a consortium of Private Equity players had their bid for Healthscope accepted by the Board following an increase in their offer to \$6.27 and the Board of Mitchell Communication also accepted a bid from UK media group Aegis valuing the company at \$363m. In the resources sector a rally in the Coal sector started after Banpu of Thailand bid for the balance of Centennial Coal. In other news, reporting season commenced with GUD and Alesco both reporting results in line with earlier guidance while Boral slightly upgraded their guidance but announced asset write-downs of \$289m and a \$490m capital raising and Adelaide Brighton upgraded their first half result on the back of strong demand for cement and lime driven by increased demand in the mining sector.

Portfolio Performance & Strategy

The Small Cap Fund gained +4.3% over the month, thereby recovering much of the losses suffered in the June quarter. For the month, the Fund benefited from good performances by Tutt Bryant and Mosaic Oil following takeover bids for both companies and from Coventry Group, Credit Corp and Thorn Group. The Fund's result was particularly good given its very low weighting to the highly cyclical mining and mining services sectors which rallied strongly over the month.

During the month Graincorp announced a merger with fellow agricultural concern AWB. The merger is to be implemented by a nil premium scrip merger, with Graincorp offering 5.75 shares for each AWB share. The merger will generate significant savings of \$40m from combining both companies trading businesses and the elimination of duplicated overheads. For Graincorp this expedites its move into WA and SA by giving the company access to AWB's grain pools in those states and gives them an overseas trading presence with significant customer connections. It also diversifies the company's earnings stream by adding AWB's Landmark operation.

Like several small caps, Coventry Group had fallen to very depressed levels during the GFC. The stock reversed some of these losses during July when it rallied strongly after pre-releasing its FY2010 result. This release confirmed that the trend of steadily improving profits has continued following the interruptions caused by the company's warehouse move. With its release, Coventry's management gave guidance as to the EBIT margins they believe the company will earn over time, and indicated a significantly higher profit in FY2011. Despite the recent rally the stock is still very cheap trading on a PE of 8 times 2011 earnings, a yield of over 7% and a significant discount to NTA of \$3.38 with a net cash balance sheet.

During the month, Tutt Bryant rallied 44% following a takeover bid from majority shareholder Tat Hong Group from Singapore. Tutt Bryant is one of Australia's two leading heavy lift crane operators, the exclusive importer and distributor of niche industrial equipment and a hirer of small industrial equipment. With the bid pitched at a premium to NTA and a significant premium to the market price before the bid, we believe this is an attractive offer and a good outcome for the Fund.

Oil and Gas concern Mosaic Oil also rallied over the month following a takeover bid from AGL. Mosaic Oil is one of the Fund's few oil investments and we were attracted to it by the strategic nature of its depleted Silver Springs gas wells and associated infrastructure, which were previously attributed very little value by the market. The company has proved these fields can be re-used to store ramp-up gas generated in Queensland by coal seam gas producers. The current bid is a good outcome for the Fund being a 90% premium to the share price before the bid.

Given the current uncertain environment we continue to favour companies that have relatively defensive earnings, strong cash flows and a strong market position and which are reasonably priced. We remain cautious on the more cyclical mining sector given the slowing Chinese economy and the difficulties facing the European economies. We are also currently holding a high cash weighting and assessing many potential opportunities.

Fund Report as at 31 July 2010

Performance Statistics

Unit Price

Application	\$0.9158
Redemption	\$0.9112

Fund Start Date	1 February 2007
Fund Size	\$13 million

Period	Fund Return*	Benchmark**
1 month	+4.3%	+5.2%
3 months	-2.6%	-7.0%
6 months	+0.8%	-1.1%
1 Year	+20.1%	+7.3%
2 Years [^]	+7.5%	-6.0%
3 Years [^]	-1.8%	-12.4%
Since inception	+2.1%	-7.0%

[^] % Performance per annum

* Fund Returns are calculated net of management fees, and assuming all distributions are re-invested.

** The benchmark for this Fund is the Small Ords Accum. Index

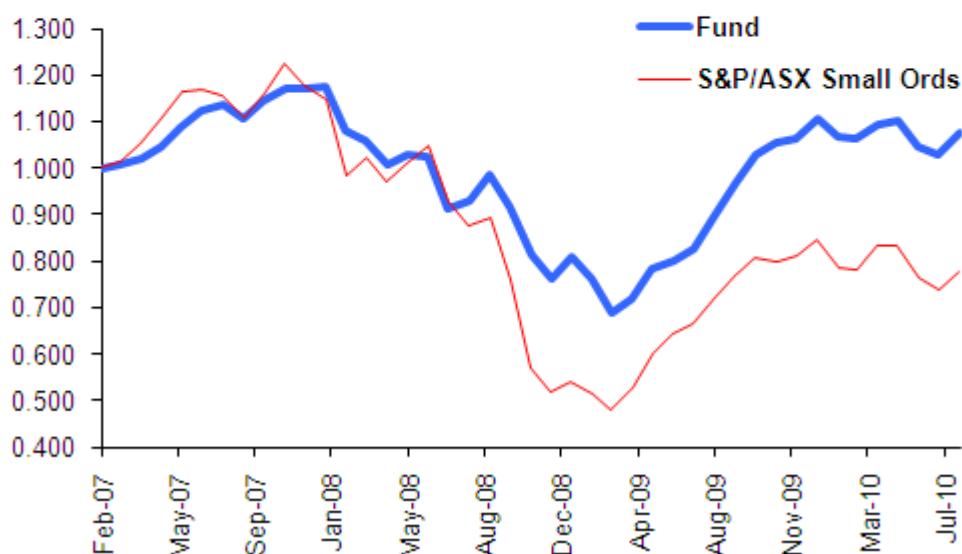
Portfolio	% of Fund
Amalgamated Holdings	4.99%
Metcash	4.87%
Energy Developments	3.52%
Sky City	3.51%
Salmat	3.48%
Goodman Fielder	3.29%
Tatts Group	3.24%
Thorn Group	3.21%
Cabcharge	3.16%
Credit Corp	3.07%
Top Ten Stocks	36.34%
Other Stocks	52.54%
Cash	11.12%
Total	100.0%

Small Cap Fund

Small Cap Fund (IMCAPS) - July 2010

Performance

IMCAPS vs ASX Small Ords Accumulation Index



* **Other Stocks held include:** Spotless Group, Ridley Corp, Coventry Group, McPherson's, Prime Media, Over Fifty Group, Ansell, ConnectEast, Graincorp, GWA International and others.

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