

SAM Sustainability Leaders Australia Fund

**Fund Manager
And Responsible**

Entity

Vanguard Investments
Australia Ltd,
ABN 72 072 881 086

Investment approach

Seeks to capture the
performance of
Australia's Sustainability
Leaders.

SAM believes that, over
time, these companies
will outperform the
broader Australian equity
markets.

**SAM
Sustainable Asset
Management**

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Performance Attribution

In this quarterly report we examine new performance attribution that was conducted for the period of the two years to end 2003. During this period the Fund returned 1.30% per annum which represented an underperformance of 0.95% compared to the S&P/ASX 200 return of 2.25% per annum.

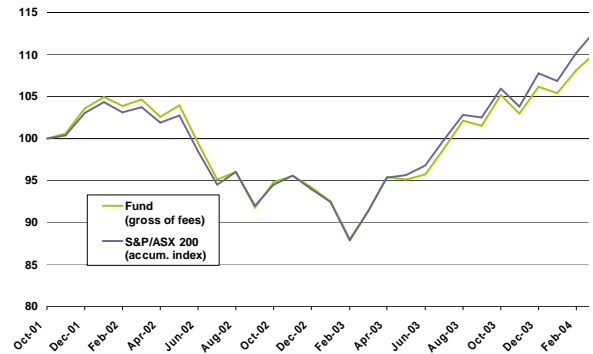
The portfolio construction approach for the Fund was designed to be similar to the Dow Jones Sustainability Index in that it is a best of sector approach and the percentage weightings of the industry sectors are largely similar to those of widely used mainstream indices. The chart entitled "Breakdown by Sector" shows the Industry weightings of the Fund versus the S&P/ASX 200 and they can be seen to be broadly in line. Therefore we would not expect the performance contribution from Industry sector to be too high and, in fact, the performance contribution was shown to be +0.16% per annum.

The other risk factor that exists in the Fund is a

Top Ten Holdings

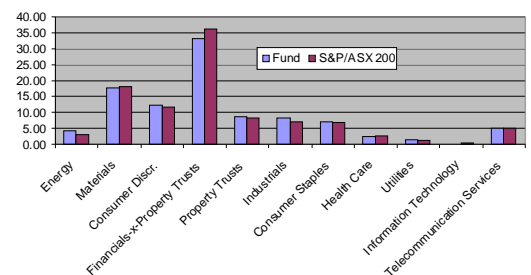
National Australia Bank	8.3%
BHP Billiton	8.0%
NewsCorp (incl. Preference Shares)	7.6%
ANZ Bank	6.7%
Westpac Bank	6.0%
Telstra Corporation	5.0%
St. George Bank	2.9%
Rio Tinto	2.3%
Coles Myer	2.1%
Wesfarmers	2.0%

Performance Chart since Inception as at 31 March 2004
Source: SAM



Net asset value:	\$1.0155
Purchase:	\$1.0176
Withdrawal:	\$1.0134
Buy/Sell Spread:	+/-0.20%
MER:	0.70% p.a.
Total Fund Size:	\$82.9 million

Breakdown by Sector



Key performance data as at 31 March 2004

	1 Mth	3 Mths	12 Mths	S. Incept.(pa) *
FUND Net Return	1.78%	3.52%	19.72%	3.43%
FUND Gross return	1.85%	3.70%	20.56%	4.15%
S&P / ASX 200 Accumulation Index	2.32%	4.67%	23.41%	5.18%

*Commencement 14 November 2001

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slight underweight to small cap stocks. Small caps have performed better than big cap stocks in the last 2 years and this was shown to cost the portfolio -0.24% per annum.

The remainder, and therefore majority, of the underperformance comes from stock selection and this raises the question of the efficacy of sustainability as a stock selecting methodology. To investigate this question further we have analysed each "position" taken in each of 2002 and 2003 and categorised them as either adding value ($>0.01\%$ contribution), neutral or subtracting value ($<-0.01\%$ contribution).

"Contribution" is a function of active weight and index-relative performance while the "position" was in place. Within each calendar year there are around 260 positions, as we start each year with roughly 70 stocks held (and 130 not held) and then in the fourth quarter we rebalance to reflect the new scores and rankings. If we replace 20 of the stocks (a typical result), we end up with 90 held (the original 70 and the 20 added at the rebalance) and 170 not held at some point during the year (the original 130, the 20 dropped at the rebalance and about another 20 arising from changes to the Top 200 during the year).

The results are equivocal. Over the two year period, the number of winning and losing positions was almost equal. Total losing = 179 ; Total winning = 176.

Since the number of "winners" is almost the same as the number of "losers" this tells us that if we had bet the same amount on each position we could have expected to produce the same return as the S&P/ASX 200. However, the fact is that the average loss associated with losing positions was more than the average gain associated with winning positions.

The potential for this situation to arise is particularly strong in the highly skewed "Australian market" where the Top 10 stocks account for 48% by market capitalisation of the Top 200. In the last quarter alone one single position – the lack of holding in the Commonwealth Bank – caused the Fund to lose 68 basis points. This was the single biggest factor in the Fund's underperformance of 97 basis points in the last quarter.

Clearly it is important then that the "success rate" of sustainability as the primary stock selection criteria improve from its current 50% in the years ahead, but also we would hope to see some "mean reversion" in the relative sizes of the average win and loss positions. If this occurs we could expect to see some early recovery in the recent underperformance.

Erratum: In the last Quarterly Report we erroneously referred to the "Sustainable Company of the Year Award" as an award made by the Ethical Investment Association. In fact this award is made by Ethical Investor magazine.

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