

Australian Ethical Super Annual Report

Year ended 30 June 2012

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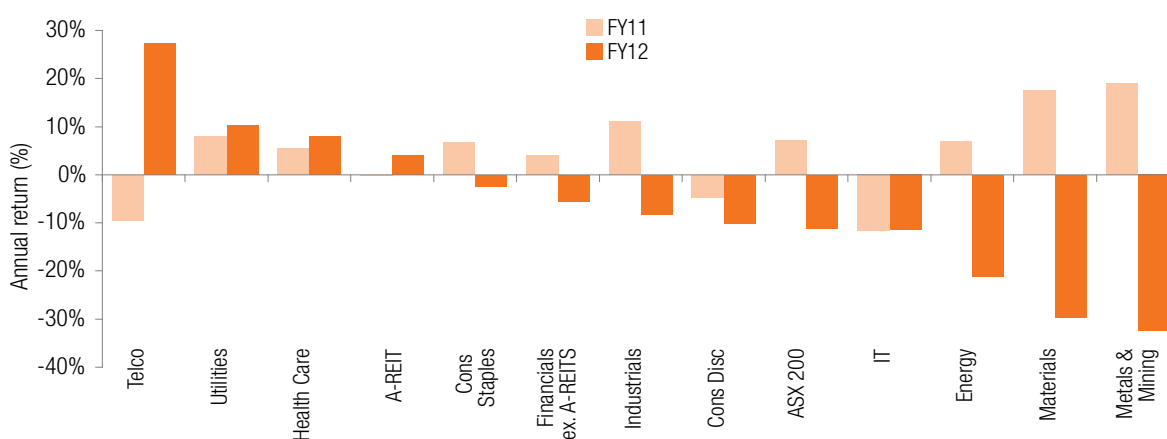
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Volatility makes stock selection the key

This article first appeared in the Member Newsletter sent to all members with their Annual Statements in September 2012.

The Australian sharemarket (as measured by the S&P/ASX 200 Index) lost ground in the 12 months ending 30 June 2012, with a return of negative 11.1%. Not all sectors fared equally as can be seen in the chart below. 'Cyclical' sectors such as Metals & Mining (-32.5%), Energy (-21.1%) and IT (-11.4%) were shunned in favour of 'defensive' sectors, like Telecommunications (+27.3%), Utilities (+10.3%) and Health Care (+8.1%).

Various indices returns in FY11 and FY12

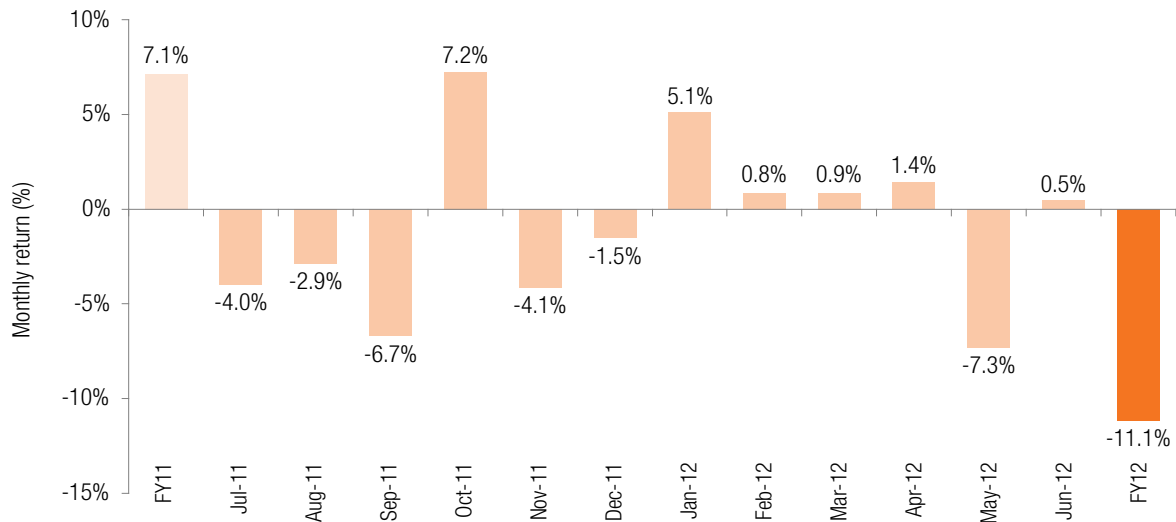


While the broader market fell 11.1% over the year, month-by-month movements were pronounced (as shown in the chart on page 3) swinging from positive 7.2% for the month of October 2011 to negative 7.3% in May 2012.

Much of this can be traced to constant shifts in investor sentiment, driven in part by economic events such as the European Union's ability to navigate its sovereign debt crisis. Events in Greece and Spain in particular were of deepening concern over the year, although the recent Greek elections brought some investor relief, with the centre-right New Democracy fending off a challenge by the anti-austerity party Syriza. Additionally, concerns about weak US jobs data and China's reported weaker growth in Gross Domestic Product, and import and export growth contributed to the volatile markets.

In Australia, the Reserve Bank of Australia cut the official cash rate on four occasions during the year (November, December, May and June) by a total of 1.25 per cent. The moves were in response to weaker than expected economic conditions and by financial year end the official cash rate stood at 3.5%. With ongoing funding pressure on Australian banks and intense competition for deposits, the banks only passed on part of the rate relief to consumers and businesses.

ASX 200 returns by month in FY12



Our view

In order to stimulate the non-mining related sectors of the Australian economy, especially housing and construction, manufacturing, education and tourism industries, which have continued to struggle, it is our view that a continued easing of monetary policy will be necessary.

Interestingly, while the domestic economy can be best described as a 'two-speed economy' – characterised by a booming mining industry in Western Australia and Queensland – the share prices of resource stocks have fared much worse than the broader market – down 32.5% for the year, reversing the previous year's 18.9% gain.

Australian Ethical Investment's Funds (in which the Super investment options invest) do not hold mining resources stocks as they do not fit The Charter. Instead, investments are skewed towards an exposure to defensive industries. As a result, our domestic equity portfolios have outperformed the broader market index over the year ending 30 June 2012.

While there really is nowhere for our equity funds to 'hide' in uncertain times, they have minimal exposure to companies with direct activities in the troubled European economies or that are reliant on discretionary consumer spending. Our healthcare investments such as Cochlear and CSL will continue to see demand for their products irrespective of what happens in Greece, our biotechs such as Alchemia and Pharmaxis continue to develop exciting new treatments for diseases, and our telco & IT companies like Oakton and SMS will continue to offer their in-demand services to domestic businesses.

We continue to place a greater emphasis on quality companies with robust business models, manageable debt position and trustworthy management. Our biotech names are mostly in the latter stages of clinical development with commercialisation typically expected in the next one to two years, and we are selectively pursuing new opportunities where we see compelling value.

David Macri

Chief Investment Officer
Australian Ethical Investment

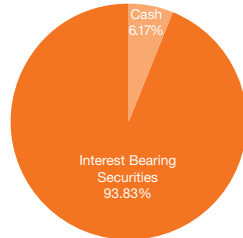
Investment options

Asset Allocations(%)* to 30 June 2012

Defensive

Performance objective:
Over 6 to 12 months, achieve returns equal to inflation

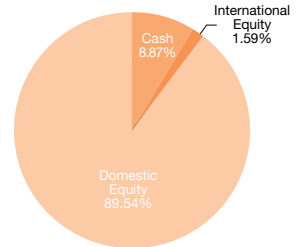
Risk measure:
Very low



Smaller Companies

Performance objective:
Over 5 to 7 years, achieve returns 5–6% above inflation

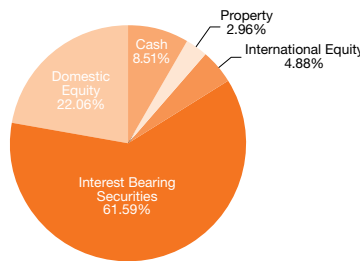
Risk measure:
High



Conservative

Performance objective:
Over 4 to 6 years, achieve returns 1% above inflation

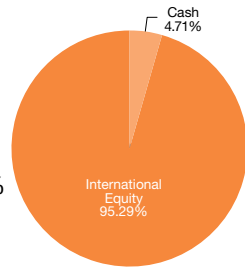
Risk measure:
Low to medium



International Shares

Performance objective:
Over 5 to 7 years, achieve returns 4.5–5.5% above inflation

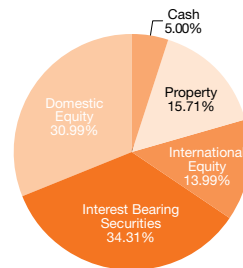
Risk measure:
High



Balanced

Performance objective:
Over 4 to 6 years, achieve returns 2.5–3.5% above inflation

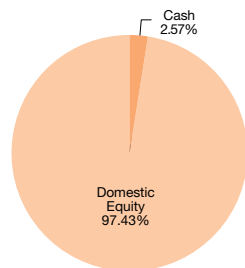
Risk measure:
Medium



Climate Advocacy

Performance objective:
Over 5 to 7 years, achieve returns 4–5% above inflation

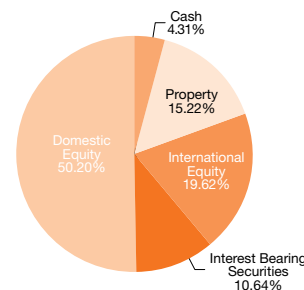
Risk measure:
High



Growth

Performance objective:
Over 5 to 7 years, achieve returns 3.5–4.5% above inflation

Risk measure:
Medium to high



* The strategic asset allocation for the Accumulation and Pension options are the same, however the actual asset allocations do vary. Please refer to the Australian Ethical website for the asset allocations for the Pension options.

Returns to 30 June 2012

Super	3 month return (%)	1 year return (%)	3 year return (%p.a.)	5 year return (%pa)	10 year return (%pa)	Since inception (%pa)
Defensive	0.8	4.3	4.2	4.0	4.2	4.0
Conservative	-0.2	1.9	n/a	n/a	n/a	3.6
Balanced	-1.6	0.3	2.2	-1.4	4.1	5.1
Growth	-2.7	-2.4	0.2	-5.1	4.2	6.3
Smaller Companies	-6.8	-4.4	2.7	-1.3	7.0	7.8
International Shares	-6.1	-15.8	-7.0	n/a	n/a	-10.7
Climate Advocacy	-3.6	-3.7	n/a	n/a	n/a	-0.5
Pension	3 month return (%)	1 year return (%)	3 year return (%p.a.)	5 year return (%pa)	10 year return (%pa)	Since inception (%pa)
Defensive	1.6	4.2	4.9	4.6	4.9	4.9
Conservative	-0.1	2.7	n/a	n/a	n/a	3.1
Balanced	2.2	0.9	3.0	-1.4	4.7	5.5
Growth	2.8	-2.8	1.1	-5.5	4.6	5.3
Smaller Companies	-0.4	-2.8	4.2	-1.1	7.8	8.0
International Shares	-0.1	-17.9	-8.0	n/a	n/a	-12.5

Past performance is not a reliable indicator of future performance. Total returns are calculated using exit prices. Total returns take into account ongoing management fees and trust or super fund expenses. The annual member fee is not included.

The total returns are based on an investment of \$10,000 at the inception of each strategy. Performance figures for each strategy assume an investment in that strategy only.

The total returns are calculated taking into account taxation on super fund earnings and capital gains. Neither the return of capital nor the performance of the super fund is guaranteed. Figures showing a period of less than one year have not been adjusted to show an annual total return. The latest available performance figures can be obtained from our website or by calling 1300 134 337.

Interests in the super fund are offered by AEI and issued by the Trustee of the Fund, Australian Ethical Superannuation Pty Ltd ABN 43 079 259 733, RSEL L0001441. The relevant PDS should be read before making an investment decision.

2012 Community Grants



As prescribed in Australian Ethical's constitution, 10% of our profit is donated to charitable, benevolent and conservation purposes as part of our contribution to a positive and sustainable society. This is one of the highest levels of corporate giving in Australia based on percentage of profits. It is something that the shareholders, staff and directors should be very proud of.

Traditionally, the grant recipients have been shortlisted by a small committee of staff members and voted on by employees and directors of Australian Ethical. The committee ensure that each shortlisted organisation or project is of the highest quality and in keeping with the Australian Ethical Charter. This year, for the first time, we invited all our shareholders to vote on which organisation or project should receive grants. Shareholder involvement was high with votes from approximately 150 people received.

Grant applications were received from almost 300 different organisations. There was a skew towards society based projects although the voting was overwhelmingly in favour of wildlife conservation.

Australian Ethical will be donating a total of \$53,325 to 11 organisations as part of its 2012 community grants scheme. This brings the total amount gifted to communities over the last 12 years to more than \$1.3 million.

This year's grants range in size from \$4,000 to \$13,325 and include donations to charities that work across Australia and overseas. The following table shows the breakdown of grant recipients for 2012.

Major grant recipient

Rainforest Rescue – Gunung Leuser National Park, North Sumatra

Rainforest Rescue provided us with a good overview of their project to save the last viable habitat of the Sumatran Orangutan through the protection of the World Heritage listed tropical rainforests of the Gunung Leuser National Park (GLNP) from deforestation and the expansion of illegal oil palm plantations. The GLNP also provides vital habitat for critically endangered species including the Sumatran Tiger, rhinoceros and elephant.

Outcomes of this project will be to remove 60 hectares of illegally planted oil palms within the



boundaries of the National Park, and replant with 60,000 rainforest trees. This work will be done by the local farming communities living alongside the GLNP, creating employment for economically disadvantaged people. These farmers already have an established co-operative where they will propagate and grow the trees in the nursery, and also monitor and patrol the site to prevent hunting and logging.

More information can be found on the website rainforestrescue.org.au/ourprojects/save-arainforest-orangutan.html

The 2012 allocation

Organisation	Project	State
Major Grant \$13,325		
Rainforest Rescue	Rainforest Rescue – Gunung Leuser National Park, North Sumatra	Queensland
Minor Grants \$4,000		
Bonorong Wildlife Sanctuary	Co-operative Eastern Quoll Breeding Programme	Tasmania
Communities @ Work	Yellow Van	ACT
Environment Victoria	Home Planet	Victoria
Free the Bear Fund	Solar Power for Sun Bears	Western Australia
Greening Australia WA	Transforming the Mortlock North	Western Australia
Gunawirra	Inner Suburbs Nutrition Project	New South Wales
Perth Advocates for the Earth	Planting for Black Cockatoos	Western Australia
Sea Turtle Foundation	Sea Turtle Field Research & Monitoring Equipment	Queensland
The Orangutan Project	Wildlife Protection Units	Western Australia
Trees for Evelyn & Atherton Tablelands	Peterson Creek Freeman Revegetation	Queensland

Changes to your super fund

Fund administration

We use a third party to provide administration services for the Australian Ethical Super Fund. These are services such as processing contributions, making benefit payments and generally managing the administration of the Fund for members.

Every five years, we review the Fund's administration arrangements to ensure that the services and costs are competitive and represent good value for Fund members. We recently completed this review and received a number of strong proposals from well qualified and reputable service providers. After reviewing these, the Trustee decided to appoint Russell Investments to provide the Fund's administration services, commencing from around April 2013. Russell already provides superannuation administration services for over 200,000 members and to superannuation funds similar to our Fund. Importantly, Russell runs its own superannuation fund, so they understand the importance of quality service and the need to look after members.

The project to move the Fund's administration from the current provider to Russell has commenced. Our intention is make sure the transition process runs smoothly and has minimal impact on members. In future communications, we will update you on the progress of the transition and provide you with further information on Russell.

MySuper

You may have heard about the Commonwealth Government's MySuper initiative (see strongersuper.treasury.gov.au).

The Government intends that from 1 July 2013, funds will be able to offer a simple, low cost default superannuation product called MySuper to improve the simplicity, transparency and comparability of default superannuation products.

To be able to offer a MySuper product, superannuation funds will need to be authorised by the Australian Prudential Regulation Authority ('APRA'). We are reviewing material recently released by APRA for MySuper applications and intend to seek authorisation to offer a MySuper product.

Insurance improvements

An important aspect of the MySuper reforms referred to above is that automatic death & total and permanent disablement insurance will need to be provided to members, on an opt out basis.

We will in future be providing automatic death and total and permanent disablement insurance, on an opt out basis through our new group insurer MetLife. In addition, a number of other important improvements are being introduced to our insurance arrangements:

- Transfer in terms – members wishing to rollover to the Fund will (in most circumstances) be able to obtain the same level of insurance cover, with minimal underwriting, as they have outside the Fund;
- Members will have the ability to increase their insurance cover upon a life event with minimal underwriting;
- There will be unlimited death cover and higher levels of terminal illness and TPD cover (subject to underwriting);
- An extension of TPD coverage to age 70 (from the current limit of age 65);
- Online insurance capabilities – including the ability to lodge insurance applications online.

More details will be provided as the features are implemented early in 2013.

Smaller Companies option

The Smaller Companies accumulation and pension investment options will no longer invest in international equities.

Changes to directors

On 29 August Phillip George resigned as a director of the Trustee and Steve Gibbs was appointed. Steve's details can be found on Australian Ethical's website.

Accounts

The Australian Ethical Retail Superannuation Fund financial statements for the year to 30 June 2012 are shown in abridged form below. A copy of the full accounts and the auditor's report is available to members upon request. Please phone 1300 134 337, if you would like a copy mailed to you.

Operating statement

for the year ended 30 June 2012

Investment revenue	2012 \$	2011 \$
Interest	405,965	465,720
Distributions	8,794,671	13,413,780
Changes in net market values	(13,863,858)	3,058,439
Direct investment expense	(176,639)	(131,226)
Total investment revenue	(4,812,861)	16,806,713
Contributions revenue		
Employer contributions	32,639,941	30,022,767
Member contributions	3,633,042	7,220,815
Transfers in	16,223,678	16,353,637
Total contribution revenue	52,496,661	53,597,219
Other revenue		
Management fee rebate	6,473,306	6,562,385
Other revenue	234,483	18,861
Total other revenue	6,707,789	6,581,246
Total Revenue	54,391,589	76,985,178
Less:		
General administration expenses	9,793,472	9,624,455
Surcharge tax expenses	1,174	83
Total expenses	9,794,646	9,624,538
Benefits accrued as a result of operations before income tax	44,596,943	67,360,640
Income Tax Expense	541,407	4,766,580
Benefits accrued as a result of Operations after income tax	44,055,536	62,594,060

Statement of financial position

for the year ended 30 June 2012

Investments	2012 \$	2011 \$
Units in unit trusts	361,219,511	345,924,418
Property trusts	17,747,677	16,079,079
Total Investment Assets	378,967,188	362,003,497
Other Assets		
Cash at Bank	9,058,045	13,802,803
Other Receivables	6,102,611	9,349,513
Deferred Tax Asset	5,545,026	2,685,950
Total Other Assets	20,705,682	25,838,266
Total Assets	399,672,870	387,841,763
Liabilities		
Accounts Payable	1,647,952	2,362,180
Current Tax Liabilities	792,854	747,029
Deferred Tax Liabilities	-	2,875
Total Liabilities	2,440,806	3,112,084
Net Assets available to pay Benefits	397,232,064	384,729,679
Liability for Accrued Benefits		
Allocated to members' accounts	397,217,831	384,682,338
Unallocated to members' accounts	14,233	47,341
	397,232,064	384,729,679

Things you should know

Indemnity insurance

The Trustee is covered by indemnity insurance to protect it from losses arising from claims against it. The insurance has been provided by QBE Insurance (Australia) Ltd throughout the 2011–12 financial year.

Investment managers

The Trustee uses Australian Ethical Investment Ltd as its investment manager. More than 5% of the Fund's assets were invested in Australian Ethical's funds during the year.

Derivatives

The Australian Ethical Retail Superannuation Fund does not directly use derivatives. It invests in collective investment funds managed by Australian Ethical Investment Ltd, which may use derivatives to reduce the impact of large adverse movements in currency exchange rates (foreign currency hedging). The collective investment funds may also use derivatives to manage interest rate and duration risk in fixed interest and property portfolios.

Complaints resolution

If you have any inquiries or complaints you should address them in the first instance to the Trustee on 1300 134 337 or by writing to the Complaints Officer at the address below.

If you are dissatisfied with a decision of the Trustee relating to you as a member, you may be able to lodge a complaint about the decision with the Superannuation Complaints Tribunal. The tribunal's role is to act as conciliator on such matters and, where appropriate, make determinations (including determinations overturning decisions by trustees).

The Superannuation Complaints Tribunal may be contacted on 1300 884 114.

Allotment of earnings

Australian Ethical Superannuation uses unit prices for its investment options. Once a week

a unit price is struck for each investment option and members' funds are updated in line with the movement in their investment option unit price. Movements in unit price reflect movements in the value of an investment option's assets as well as amounts payable by the investment option for fees and expenses.

Eligible rollover fund

An eligible rollover fund is a fund established under superannuation law which accepts benefits of members from other funds in certain circumstances.

Australian Ethical Superannuation has chosen the Australian Eligible Rollover Fund as its eligible rollover fund. A member of our fund may be transferred to the eligible rollover fund:

- if they are a lost member with a balance of less than or equal to \$1000;
- if they are a lost member with a balance of more than \$5000, where they have been a lost member for a period of five years or more;
- if they have a balance of less than \$3000 and no contribution has been received from or on behalf of the member for a period of two years.

A member is regarded as lost if at least two written communications have been sent by the Fund to a member's last known address and they are returned unclaimed.

We will attempt to contact relevant members before they are transferred to the eligible rollover fund.

Being transferred to the Australian Eligible Rollover Fund may affect your benefits because you will cease to be a member of the Australian Ethical Retail Superannuation Fund. If you hold insurance cover through the Fund, this insurance will cease. A member transferred to the eligible rollover fund will be subject to the governing rules of that fund and a different fee structure and investment strategy will apply. If your benefit is transferred to the eligible rollover fund, you may require the following contact details:

Australian Eligible Rollover Fund
Locked Bag 5429
Parramatta NSW 2124
1800 677 424

Contact us

We help people invest their super and savings in an environmentally and socially positive way.

Phone: 1300 134 337
Email: members@australianethical.com.au
Web: australianethical.com.au
Twitter: @austethical
Facebook: [australianethical](https://www.facebook.com/australianethical)

The information contained in this report is general information only. It doesn't take into account your individual objectives, financial situation or needs. Before making any investment decisions you should assess whether the information is appropriate to your circumstances. Interests in the Superannuation Fund (registration number R1004731) are offered by Australian Ethical Investment Ltd ABN 47 003 188 930, AFSL 229949 and issued by the Trustee of the Fund, Australian Ethical Superannuation Pty Ltd ABN 43 079 259 733, RSEL L0001441. A product disclosure statement is available from our website australianethical.com.au or by calling 1300 134 337 and should be considered before deciding whether to acquire, or to continue to hold, interests in the Fund.

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Risk measures are based on the Standard Risk Measure Guidelines issued by the FSC and ASFA.