



15/01/2010

<i>Unaudited results for 12 month period ending 31 Dec 2009</i>						
		Other currency equivalent				
		USD	EUR	GBP	BWP	ZAR
12 months	Net to investors	70.3%	67.5%	61.5%	58.0%	48.2%
	MSCI AC World Index	26.2%				
12.5 years-compounded (22 Apr 1997 - 31 Dec 2009)	Investment officer (full service track record - net to investors)	10.8%	9.3%	10.9%	15.9%	16.4%
	MSCI AC World Index	2.6%				
	NAV	\$165.27				

*"Experience: that most brutal of teachers. But you learn, my God do you learn" - C. S. Lewis*

*Letter to investors:*

Nobody enjoys being ignored and I am no different; especially when those ignoring me are our investors. Yet, in this case I don't mind. When I recently suggested that you take out any funds, from Baobab, you might need, you all ignored the suggestion. Some of you actually added to and in one case even doubled your investment. I appreciate the vote of confidence and always enjoy watching every brick being laid down in building our company; your bricks consist of your hard earned money that you give to us to manage and my bricks are made up of long term investment returns. As I have often said, when measuring my performance, *the bottom line is the bottom line* and 2009 makes for a welcome change to 2008; for a comprehensive, in-depth and extremely thorough discussion of our experience in 2008, please see the C.S. Lewis quote above.

Please note that we opened Baobab to new investors, for the first time in four years. So if any of your friends and family qualifies as sophisticated investors and are people you respect and admire then you should think about having them join our business.

There are also a number of very significant changes afoot, which I will cover in detail in the upcoming annual report. I will also do my customary round of phone calls early in the year.

As you know, we are generally reserved about discussing our general views and certainly extremely reluctant to discuss any specific investment ideas unless there is something in it for us. However, as a means of ensuring that we all stay in the right frame of mind, which is to prepare for the worst and hope for the best, please note the following.

**SUCKER PUNCH**

*"In urban slang it does not just mean an unannounced or unexpected attack. A true sucker punch is quite a bit more complex. It primarily involves a closed fist contacting the soft underbelly of a person (beneath the rib cage) at a high velocity, causing the ensuing force to press upward on the victim's diaphragm, leading to a sudden expulsion of air from the victim's mouth and lungs. This opening blow leaves the victim open to various other attacks." -www.urbandictionary.com*

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LEGAL Management Company: Cherubim Ventures (Pty) Ltd Reg CO.2003/5941  
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Company Secretary: Corporate Services (Pty) Ltd  
Baobab Global Fund is a hedge fund and may not do business with the public. It can only do business with institutions and wealthy individuals.

The only way of preventing a sucker punch is to escalate your preparedness for not getting suckered, with the resulting peak in your preparedness at the time circumstances generally indicate that it is the least likely moment for a punch to be thrown. What makes a sucker punch increasingly dangerous is that 9 out of 10 times you will only realise you have been sucker punched after waking up on the floor and after having been stripped of everything of real value. You are pretty much at the mercy of the puncher.

So that is why with banks stabilized, the economy picking up and Asian exports on the increase, we don't feel its time to celebrate, just yet. Rather we believe it is the perfect time for a sucker punch.

*"Purchase: to obtain by paying money or its equivalent"* - Merriam Webster Dictionary

The Federal Reserve and other similar global institutions have created money at a rapid rate by doing pretty much what I am doing now, tapping away on a keyboard. It "**purchased**" about \$1 trillion of securities from the banking system in 2009 and the banks have now used this newly created \$1 trillion of money to repair their balance sheets. Instead of the banks lending excess funds "into" the real economy they decided to apply it to their own treasury operations by mostly trading in things like the stock market and the biggest casino of them all, the derivatives market. In my view the derivatives market is the *mother of all casinos*, in every respect. The most recent report from the *Comptroller of the Currency*, seems to suggest that the *mother of all casinos* has now successfully completed the first year where the notional value was more than \$200 trillion for the entire year. Please note that this was "only" a \$20 trillion industry 10 years ago; Vegas, eat your heart out.

Now tie this in with the fact that most of the 2008 and 2009 derivatives losses were in the *credit* derivatives market, which only makes up 6.4% of the total market. *Interest rate* derivatives, on the other hand, make up a whopping 85%, and together with 7.6% of *foreign exchange* derivatives, means 93% of the total market will be affected by extreme volatility of interest rates in the global markets. It would be foolish to expect a "quiet" interest rate market in the near term.

Not to worry, says the comptroller of the currency, because of the following reasons:

1. There are a number of other providers of derivatives products whose activity is not reflected in its report. I am not sure which is the most worrying, the fact that there is a big enough market out there consisting of "other" providers that can offset a \$200 trillion market or the fact that I think the comptroller could very well be wrong.
2. "Because the highly specialized business of structuring, trading, and managing derivatives transactions requires sophisticated tools and expertise, derivatives activity is concentrated in those institutions that have the resources needed to be able to operate this business in a safe and sound manner". The *trust the big boys, they know what they are doing* line has just never carried it with us. It usually is simply an indication that there is an opportunity to profit from their mistakes. Also, with 97% of the \$200 trillion sitting with the top 5 banks and 88% with the top four, the most popular argument, that these banks layed off their risk, simply spells, *we are all in this together*. Now you know the real reason, why JP Morgan, Goldman, Citi and Bank of America are too big to fail; they are the US derivatives market, which is a pretty important piece of the US and global banking pie.
3. The third and always my favorite reason put forward by the comptroller is the fact that the "OCC and other supervisors have examiners on-site at the largest banks to continuously evaluate the credit, market, operation, reputation, and compliance risks of derivatives activities." Never in all of human history has it generally yielded a satisfactory outcome when you get a guy earning \$100,000 per year to watch the guy that is earning more than \$1m (average 2009 pay for Goldman employees) per year.

So the derivatives issue is obviously still a major concern to us. Also, when you have the central banks starting to tinker with the capital ratios of the banks as reported in the FT this week, "Top banks invited to BIS talks amid new risk fears" then we get even more worried. By the way, I find the use of the word *invited* rather interesting. It has the same ring to it as when the headmaster, or the tax man or your father-in-law to be "invites" you for a chat. There is an uncomfortably high probability that the outcome might be fairly serious and in the banks' case the end result could be "tightening" and when that starts to happen, especially in an unexpected way, then all bets are off. It only serves as a good layup for a sucker punch.

Please don't misunderstand my mood, these are very interesting developments and considering it against the broader history of financial markets we can expect more, not less, volatility. For me and my *little wolfpack* that I hunt with, it spells opportunity. So when we find opportunities, and we are still finding some, we do not hesitate to deploy our cash. Yet, I spend an awful lot of energy on ensuring that in 2010 we do not fall victim to the sucker punch and are rather well prepared, to pick some pockets!

God Speed,

A handwritten signature in black ink, appearing to read 'M. van Blerk', with a stylized, cursive flourish extending upwards and to the right.

Martin van Blerk