

Core Portfolio

Sterling Quarterly Report 31 March 2009

Objective: To achieve a real return in excess of risk free sterling cash interest rates over a three to five year period. Performance is targeted through the strategic asset allocation of a diversified multi asset class investment. This means important changes will regularly be made to reflect changing market conditions. Asset allocation may be made across all of the major asset classes being cash, bonds, commercial property, equities and alternative investments. Our philosophy is to invest into passive investments (investment performance vehicles that mirror the respective market) through our core portfolio wherever possible.

Cash: The global economic environment deteriorated further during the first quarter of 2009 and the world's major governments and policy makers have the challenging task of stimulating their domestic economies. The UK base rate has been cut to an all time low of 0.50% but it has become clear standard monetary policy tactics are inadequate to arrest the current rate of economic decline. Quantitative easing has been introduced with the objective of ultimately boosting household and corporate spending. If it works, inflation will return alongside rising interest rates.

Bonds: The most significant news for bond markets this quarter was the announcement by a number of major governments – including the UK - that they were adopting unconventional strategies in the form of quantitative easing. The term refers to a policy by which the government buys bonds and/or corporate securities in order to try and drive down the longer end of the yield curve and reduce borrowing costs. Policies have also been introduced to eliminate toxic assets on banks' balance sheets.

Not surprisingly, the fixed income markets reacted positively to the news – with the ten-year gilt experiencing the largest one-day rally since the Bank of England was granted independence in 1997. This positive sentiment had a lesser impact on the corporate bond market, where prices fell over the quarter on continued risk aversion and deleveraging by participants. As a consequence, at the end of the first three months of 2009, UK government bond prices were down by 0.23%, having recovered most of their losses after a poor start to the year; whereas sterling corporate bonds fell 8.18%. This underperformance of the corporate sector can be largely attributed to the market's significant weighting in financials, whose subordinated debt continued to sell-off over concerns that some issues may be restructured via debt-for-equity swaps.

In this context, the two actively managed investment grade bond funds we are invested in have performed relatively well, falling by 0.59% and 1.89%. We currently have a 30% allocation to bonds within the core portfolio.

We remain confident that, at current levels, investment grade bonds offer good value and attractive yields, with the potential for capital gains when prices improve in the medium term.

Actual Return in 2009 YTD	0.41%
Standard Deviation^ (12 month rolling)	0.44%
Current Weighting	50.15%

Actual Return in 2009 YTD	-0.70%
Standard Deviation^	8.81%
Current Weighting	29.96%

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Equities: As expected, equity markets continued to follow a volatile and downward path during the first quarter, with the MSCI falling by a further 10.6% in dollar terms and 12% in sterling. This was despite a rally in March when markets saw a tentative improvement in some leading indicators as a positive sign that policy actions were starting to work.

The degree of fiscal, monetary and quantitative easing that governments are applying, as most recently evidenced by the G20 outcome, is unprecedented but the impact remains uncertain both in terms of the size and the nature required. Consequently, we expect markets to remain volatile and renewed downward pressure can be expected should the eventual outcome of these actions become doubtful. During the quarter we reduced the equity allocation to nil to protect the portfolio against the potential for further downside.

Looking ahead, it remains to be seen whether or not the positive sentiment witnessed in March is part of a lengthy bottoming process and this will be determined by economic data over the next few months. Some consolidation can be expected sooner rather than later, especially if quarter one corporate earnings disappoint, with forecasts already set at low levels.

In order to commence reinvesting we will require confidence of a more sustained recovery and this in turn will require firmer signs of a brighter outlook than are currently available.

Property: The investment committee has continued to allocate a zero weighting to property in the current environment. The performance for property during the first quarter as measured by the investment property data bank UK all property sector index was -6%. As the economy continues to remain challenging, we predict property will likewise continue to suffer in this environment and investors are unlikely to be rewarded above cash, even with the very low cash rates available. Therefore, we continue to watch the market for signs of a recovery but do not feel ready to invest yet.

Actual Return in 2009 YTD	-19.87%
Standard Deviation[^]	21.99%
Current Weighting	0.00%

Actual Return in 2009 YTD	0.00%
Standard Deviation[^]	0.00%
Current Weighting[*]	0.00%

^{*} Asset class exited on 19 February 2008

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Alternative Investments: **Hedge funds:** The much anticipated Darwinian process within the hedge fund arena whereby the weakest strategies fail has been evident although, as one may expect in such an opaque industry, this has been far from clear cut. Fewer players chasing trading opportunities will likely benefit from reduced competition and the unprecedented capital market disruption through late 2008 has eased somewhat, even if volatility has not. All of this has helped the broad hedge fund industry to post positive returns for the quarter with the HFRX Global Hedge Fund Index returning 0.80% for the year to 31 March. We have taken the opportunity to further reduce our exposure to the asset class by selling into this relative strength. Restrictive dealing terms for hedge funds and extended settlement periods, that were imposed by many managers following heavy redemption levels due to investor nervousness, have begun to ease and a clearer picture will undoubtedly emerge about the state of the industry going forward. Nevertheless, the big question of future regulation remains unanswered with many governments believing action is required.

Commodities: Sterling-referenced broad commodity returns, as shown by the Dow Jones AIG Commodity Index gaining 0.68% through the quarter, mask interesting dynamics within the asset class. The quarter was dominated by the governments of major economies seeking solutions to the global recessionary environment. Massive Keynesian stimulus announced by the US and China has helped to support industrial metals as production data improves. Global oil prices have also received a boon from this news with the benchmark West Texas Intermediate gaining 11.3% over the first quarter. Gold reinforced its status as the backstop asset in times of crisis with a 4% US dollar gain over the same period and significant investor flows through the quarter as equity markets gyrated wildly.

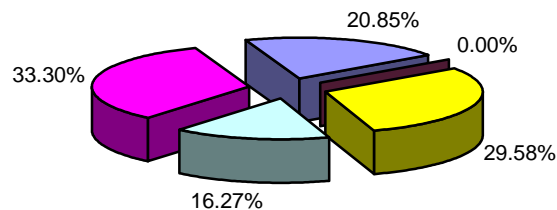
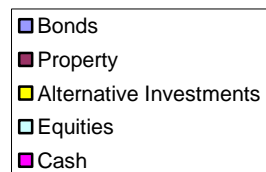
Manager's Comment:

We entered 2009 very nervous of the fast deteriorating global macroeconomic environment. It was clear corporate news flow would be weak and the prospect of rising unemployment would be an issue to focus the minds of policy makers around the world. To their credit we have witnessed an unprecedented coordinated monetary and fiscal response, which has left investors with no doubts about their determination to remedy the position. Where doubts do lie is whether the response is adequate enough or whether the action being taken is simply stoking up a wave of further problems to come. This ambiguity is leading to volatile markets and has led us, as managers, to continue focusing on capital preservation.

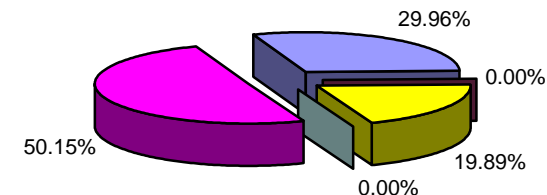
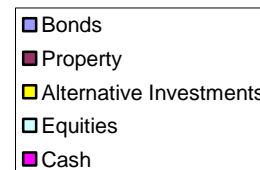
Actual Return in 2009 YTD	10.18%
Standard Deviation^	15.85%
Current Weighting	19.89%

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Quarter 4 - Asset Allocation



Quarter 1 - Asset Allocation



Performance Versus Benchmark:

	2005	2006	2007	2008	2009 YTD	Rolling 12 Months Return	Since Inception**
Total Model Portfolio Performance	10.21%	8.58%	2.01%	-18.96%	0.03%	-14.60%	0.77%
Cash Rate* (benchmark)	4.49%	4.48%	5.39%	4.64%	0.41%	3.75%	21.34%
Standard Deviation^	4.15%	3.56%	5.46%	9.12%	N/A	9.27%	6.42%

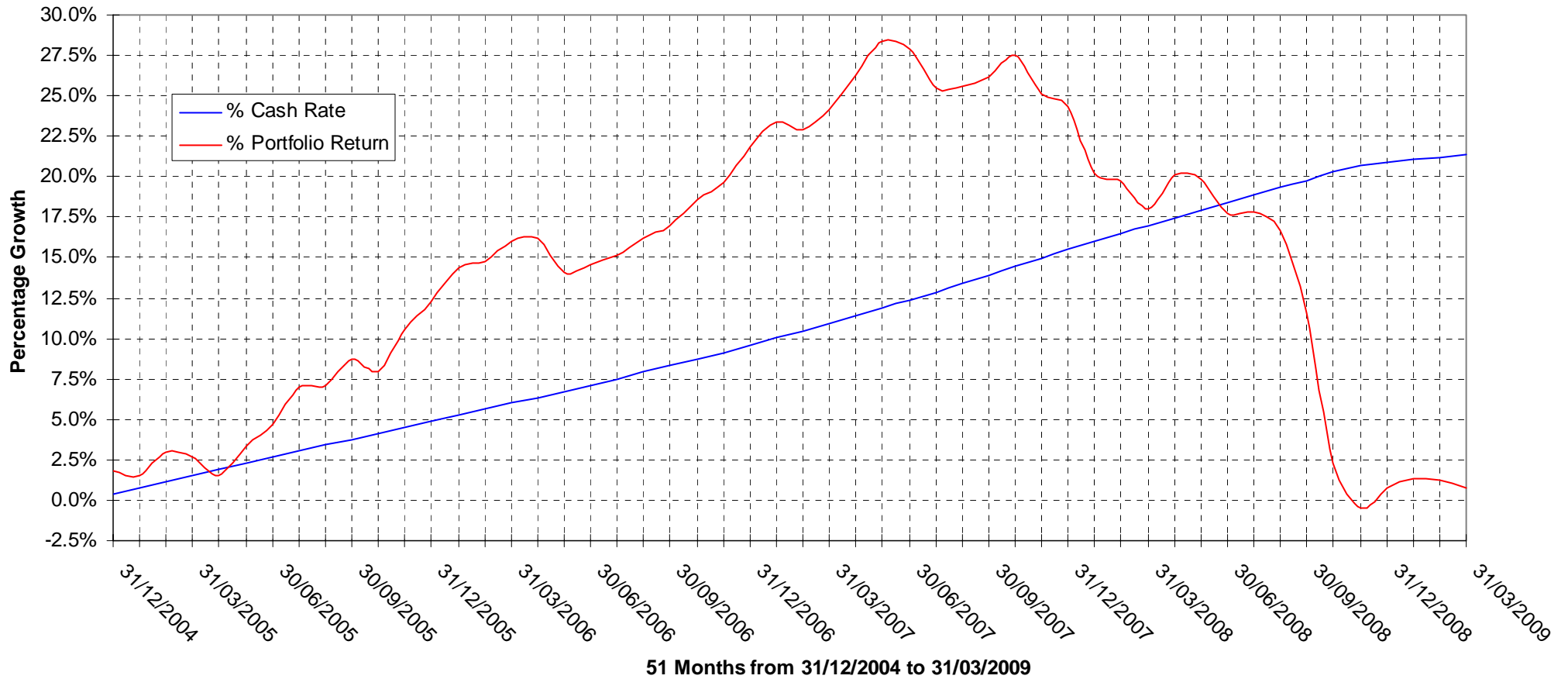
Performance figures are for the sterling core portfolio model (based on income reinvested and gross of fees).

* Cash rate is based on 3 month LIBID

** Launch Date - 1 December 2004

^ Standard Deviation is a measure of how widely "spread out" the returns of an investment are. The more spread out the returns are, the bigger and more frequent the losses on that investment. An investment's return over a year will be within one standard deviation of its expected return roughly two-thirds of the time, and within two standard deviations roughly 95% of the time. So, for example, if an investment has an expected return of 10%, with a standard deviation of 2%, then its return should be between 8% and 12% two-thirds of the time; and between 6% and 14%, 95% of the time. From November 2006 this is the annualised standard deviation of the returns for the core portfolio model.

Percentage Growth Return in GBP



Performance figures are for the sterling core portfolio model (based on income reinvested and gross of fees).

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Where daily prices are not available for valuation or performance measurement purposes, individual holdings within the core portfolio will be valued using the last available price. The value of your investments and the income from them can fall as well as rise and you may not get back the original amount invested. Exchange rate changes may affect the value of investments. Past performance is not necessarily a guide to future performance.

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Source: All data has been provided by Fairbairn Private Bank and Bloomberg.