

COASTAL MAGNUM

Diversified performance Fund

US Disaster - Financial Market Crisis

We at Coastal are shocked by the tragic events in the US and express our sympathy and condolences to all of the people affected.

The financial markets are in a state of panic. Some Asian and most European bourses have remained open and many have recorded sharp declines. In view of the market conditions, we believe it is our duty to inform you how this may affect the Fund.

As at the beginning of September, approximately 10 % of the Fund was held in cash or represented by the redemption proceeds due from certain hedge funds from which we have withdrawn but have not yet received or reinvested. The other 90 % was invested across some 22 hedge funds, of which around 70% by value are invested in more conservative "market neutral" strategies and the balance in more opportunistic long-short strategies. The maximum exposure to any single fund is approximately 8.5% of the total portfolio.

We have received feedback from a number of the hedge fund managers, but it is too soon to determine the overall impact on the Fund. What we can say is this:

12 of the 22 managers with which the Fund invests are located in New York city. Of these, to the best of our knowledge, none were located in the World Trade Centre. We received communications from 8 of these New York managers confirming that their staff, offices and physical records are unharmed, and that their prime brokers (including Morgan Stanley and Bear Stearns) have assured them of no loss of functionality. All of the hedge fund records including shareholder details are in any case maintained at the offices of the independent fund administrators, located in variety of jurisdictions far from New York including Bermuda, the Cayman Islands, the Bahamas and Dublin. Our Fund's own records are maintained in both Sydney and Hong Kong.

One of our hedge fund managers that specialises in mortgage-backed securities is checking whether any of the securities held are collateralised by any of the buildings destroyed, but pointed out that in any case bond holders would be compensated by the requisite property insurance which includes cover for loss caused by terrorist attack.

As a general observation, we are perhaps less concerned by the decline in market values than by the impact on spreads of secondary securities such as mortgage backed and convertible issues to the benchmark government securities used to hedge them. In a panic, there is invariably a "flight to quality" and spreads widen, which can result in some revaluation losses. As market conditions stabilise over time, however, spreads invariably narrow and generally the revaluation losses are recovered. This may be a matter of just a few weeks. Spreads widening may potentially affect around half the portfolio and the order of magnitude will vary from hedge fund to hedge fund and may range from less than -2% to as much as -7 or -10%.

As suggested, it is too soon to tell of the overall impact on performance given that the US securities markets will remain closed until Friday. We will update performance estimates as they come to hand on our website www.coastalfunds.com else please call our information line, 1-800-247776 should you not have web access.

Sincerely yours

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Sydney, September 13, 2001

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