

■ PERFORMANCE UPDATE

ARCANA PROVIDENT LIMITED

Dear Investor

As we previously reported to you in February this year, the world's financial markets have been affected by a significant liquidity crisis. The initial trigger to this liquidity crisis was a downgrading of the sub-prime mortgage market in the US. In Australia, the sub-prime loan market is referred to as "non-conforming loans" and generally indicates credit given to those who do not meet the typical standards of the lender, that is, they may have a poor credit history. To compensate for this non-conformity, lenders usually charge a higher rate of interest.

The sub-prime crisis commenced when some large and prominent US Hedge Funds collapsed as their assets were devalued. From that point the markets, as they often do, panicked, which has led to losses in other investment sectors including the stock market and even full investment grade securities.

Currently it appears there will be significant losses as the liquidity crisis continues to effect other investments of the Pythagoras fund (the fund). Investment deals that were designed to help the fund during this time were unable to be ratified. Other underlying investments already effected by the crisis have also been forced to continually liquidate their assets into illiquid markets. As you can appreciate, market conditions are changing constantly and we are trying to pass on any relevant information as it is received. This liquidity crisis is one of the worst economic events that has occurred in recent times and has/will have a flow on effect for world economies for some time to come.

Despite the fact that the fund was well diversified amongst many different types of Hedge Funds, many of which continue to make returns, the sheer panic of the markets has meant some funds (even those not related to sub-prime) have incurred significant losses, and the actual extent of some of these losses continues to remain indeterminable.

Additionally, due to the indeterminable nature of these assets, and the almost unprecedented volatility in the Australian Dollar the fund has been unable to maintain its Foreign Exchange hedging position.

The widespread effect of this market volatility has meant that we continue to be unable to ascertain the true impact of these events on Arcana's NAV. The calculation of the NAV has been suspended pending the receipt of definitive information in respect to the valuation of these investments from the underlying managers. Subscriptions and redemptions have also been suspended until the NAV calculation resumes.

In an attempt to progress this situation the directors and the Fund Manager have met to ratify a conservative (written down) valuation for these assets in the absence of further information.

Although a policy has been agreed, it must be noted that the number of investments yet to report final figures to the fund means that the NAV will continue to be an estimate for an indefinite period of time and we do not believe this situation will be resolved within the next year.

This report will firstly provide an estimated NAV as at 31 March 2008, however, it must be noted that this is an estimate only and that the final price determined by the Administrator or the final price received through a redemption of the fund, may vary over time. The current NAV estimate for 31 March 2008 is \$0.80 per share. This estimate is designed to provide a guide only, pending final valuations.

Following this estimate, conservative valuations will be struck by the Administrator in the coming months for 31 July 2007, 31 August 2007, 31 December, 2007 and 31 March, 2008 and will be provided in the next report. This means that any subsequent adjustments up or down will be brought to bear in the month they are ascertained as opposed to the month in which they may have occurred. Provided there is enough liquidity, all redemptions and subscriptions posted from 1 September, 2007 to 31 December, 2007 shall be processed at the final 31 December, 2007 NAV and all redemptions and subscriptions posted from 1 January, 2008 to 31 March, 2008 shall be processed at the final 31 March, 2008 NAV.

All redemptions posted from 1 April, 2008 will be gated, which means we will only be able to process a limited number of these redemptions each month provided there is sufficient liquidity.

Therefore, redemptions sent in before the end of any given month, may not be processed at the next Valuation Day NAV. Instead, redemptions will be processed at the Valuation Day NAV of the month where sufficient funds are available and will be processed on a first-come-first-served basis. This final redemption price may not necessarily be at the same Valuation Day NAV applicable when the redemption request was sent in.

It should also be noted that the prospectus does allow for a Special Meeting of Shareholders to decide on the future of Arcana if the NAV price falls below a certain level. You may recall that the prospectus states:

“All trading, issues and redemptions will be suspended in relation to the Diversified 20 class of Share if losses are suffered that reduces the NAV to less than 50% of the highest Valuation Day NAV* per Diversified 20 Share (plus dividends).

* The highest Valuation Day NAV in this context includes dividends, as dividend distributions cause variations in the NAV.”

This condition may be triggered once final valuations are received from the Administrator, at which time voting on the future of Arcana may be conducted.

If you have any questions, please don't hesitate to contact me by phone, or by emailing me at philip.york@empyrealinvestments.com.

All general queries may be emailed to arcana@qbl.com.au.

Sincerely yours,



PHILIP M YORK
Managing Director