

Pengana Australian Equities Long Short Fund

May 2009 Update



Fund Description

The Pengana Australian Equities Long Short Fund is a long / short Australian equities strategy, with a long bias and a bottom-up fundamental approach to stock selection. The Fund targets 20 - 30 longs selected from the largest 300 stocks on the ASX and 10-15 shorts selected from the top 200. The manager has a research-based investment process to evaluate investments capable of generating target returns over the medium term, with a strong focus on cash flow generation and growth at a reasonable price. Macro and technical overlays are used to assist in portfolio construction, exposure sizing and market timing. The average net long position since inception has been 45 to 50%. The Fund aims to provide investors with an absolute return of 12 to 15% per annum over the medium term with relatively low volatility (equity type returns with lower volatility). The manager also adopts procedures to manage risk and preserve the capital of investors. The Fund is managed out of Sydney.

Fund Features

Style	Fundamental, GARP	Management Fees ¹ (monthly)	1.25% per annum
Benchmark	ASX 300 Accum Index	Performance Fees ¹ (semi-annually)	20% per annum with a high water mark
Investors	Wholesale Clients only	AUM at Month End	A\$8.03m
Minimum Initial Investment Amount	A\$100,000	Application Price at Month End	Application: A\$0.8663
Inception Date	May 2004	Redemption Price at Month End	Redemption: A\$0.8636

Fund Commentary

Fund Performance (A\$, net of fees)													
	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD
2009	2.3%	-5.8%	7.6%	4.4%	1.5%								9.7%
2008	-4.2%	-3.2%	-3.8%	7.0%	-0.4%	-8.7%	0.3%	5.1%	-4.8%	-13.5%	-10.1%	-1.0%	-32.8%
2007	1.3%	0.9%	1.2%	1.9%	3.2%	0.7%	0.4%	0.8%	2.7%	1.7%	-0.8%	-0.2%	14.5%
2006	2.1%	1.2%	4.3%	0.9%	-1.1%	2.6%	0.5%	0.1%	0.7%	3.6%	0.9%	2.1%	19.0%
2005	2.6%	-1.3%	0.2%	-0.6%	-0.8%	3.3%	0.7%	4.2%	2.6%	-0.9%	3.0%	1.8%	15.8%
2004					0.8%	1.1%	5.3%	-0.2%	2.7%	5.9%	2.9%	0.7%	20.8%

The fund commenced the month of May 44% net long, ending the month 62% net long. The average net exposure during the month was 55%. During the month we took advantage of opportunities in selected cyclical names and rebuilt exposure, despite exiting the month of April with a relatively defensive portfolio. After sundry income and all costs and fees, the net return for May 2009 was 1.4%, matching the market's for the month with 55% net equities exposure. The month end mid unit price was \$0.8650 per unit.

The ASX 300 Accumulation Index rallied 1.46% over the month of May easily digesting a further \$14.7bn of capital raisings. Strong fund flows into Asia saw the region outperform materially in the chase for beta. There was significant offshore interest in the ANZ equity raising compared to earlier Australian bank raisings, which were met with some scepticism. Increasing offshore interest in Australia and the resource sectors was confirmed as the A\$ strengthened to U\$0.80 at month end. The E&P sector was buoyed by a 32% rally in the U\$ oil price. Outperforming sectors were Materials (+7%) and Energy (+6%). Underperforming sectors were Telcos (-6%) and Healthcare (-8%).

Key Contributors / Detractors

Best performers in the long portfolio were CSR (+21%), Incitec Pivot (+27%), Peet (+14%), Toll Holdings (+19%) and Worley Parsons (+23%). Defensive long positions generally underperformed. Shorts held were reduced to one position despite the lifting of the short ban on financials. The Fund continued to benefit at the margin from ongoing deep discount equity raisings.

The Fund's residual exposure to two hybrid securities, representing 8.9% of the fund at month-end, detracted 2.2% from performance. TPI (parent to TPAPA) has been voluntarily suspended from official quotation since February as the group considers

¹ All percentages are plus GST net of reduced input tax credits. Please refer to the Information Memorandum for a more detailed explanation.

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capital structure options including reduction and refinancing of its debt and the introduction of potential cornerstone investors. The other residual exposure is ELDPA (previously FCLPA). Despite asset sales by the parent ELD, debt is not reducing as quickly as expected. It remains our intention to reduce absolute exposure to these hybrids.

Outlook

It has become increasingly clear that very few investors have been positioned for this rally in equities, particularly global cyclicals. Some lead indicators viz. stronger commodity prices, Chinese PMI and commodity imports, bulk shipping rates, credit spreads, consumer confidence (primarily from the direct benefits of a substantially lower interest rate environment), encouraging housing finance numbers and stronger than expected Australian GDP numbers, all suggest that a V-shaped recovery is on for the equity bulls. Nevertheless, the recent 25 -30% recovery in global equity markets has shifted the risk / reward equation away from fundamental investors as PE ratios expand.

The bears remain focused on a W-shaped recovery, with rising long term bond yields, deteriorating business investment, rising unemployment, increasing bad & doubtful bank debts, demanding near-term cyclical equity valuations and secondary equity issuance seen as negative indicators. Although evidence is mounting that the worst is over in this cycle, needless to say it is difficult to get strong conviction.

Although investors appear to be comfortable paying above average PERs for below trend EPS, many stocks and sectors look to have run well ahead of fundamentals. This is not uncommon as under-invested domestic and foreign equity investors come back into the market. Markets will soon require some evidence of the early signs of global economic recovery, not just slowing in the rate of deterioration of economic data. Nevertheless, given the weight of cash on the equity market sidelines, we believe that market psychology has shifted from selling rallies to buying the dips, so therefore continue to expect shallower pull-backs.

Our research suggests that despite all the signs of a resilient consumer, the outlook for business investment looks extremely challenging. We will continue to approach companies that are exposed to or service the capex of others with caution. Over the past quarter we had adopted a particularly cautious stance towards taking short positions, given the limited opportunity set. It is likely that we will resume taking short exposures as the opportunities arise.

At the time of writing the portfolio has a 62% gross and net equity market exposure (38% cash), with a higher exposure to cyclicals than last month. Selectively we continue to take advantage of equity raisings and the opportunity to re-establish positions in quality defensive companies at attractive price levels as investors rotate into more leveraged plays. Your managers are retaining a medium term long bias towards building a portfolio of high quality utilities, strongly funded less economically sensitive industrials, major banks, with a variable exposure to global and domestic cyclicals and a small exposure to AREITS.

Further Fund Information

Net Returns to 31 May 2009					
	PAELSF Net Return ²	PAELSF Gross Return ³	Cash	ASX 300 Accumulation Index	PAELSF Average Net Exposure ⁴
1 Month	1.4%	1.5%	0.2%	1.5%	55.0%
3 Months	13.9%	14.2%	0.8%	15.9%	55.7%
6 Months	8.7%	9.4%	1.7%	5.1%	57.8%
1 Year	-22.5%	-21.4%	5.1%	-29.2%	57.3%
2 Years	-22.4%	-19.3%	12.2%	-33.9%	49.9%
Since Inception	40.6%	74.7%	32.8%	40.0%	50.4%
Annualised Volatility	12.8%	13.5%	0.3%	14.8%	

² Net Performance, after all fees and charges.

³ Gross Performance excludes both management and performance fees.

⁴ Exposure is delta adjusted for derivatives and preference shares.

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Further Fund Information (cont'ed)

Risk Characteristics	
Annual Volatility	12.8%
Sharpe Ratio	0.31
Downside Deviation	9.87%
Sortino Ratio	0.40
Risk Free Rate Assumed	3.00%

Performance Contributors	
Equity Longs	3.60%
Equity Shorts	0.20%
Derivatives	0.00%
Fixed Interest	-2.20%

Portfolio Structure	
Long Positions	32
Short Positions	1
Equity Long Exposure	63.5%
Equity Short Exposure	1.2%
Net Long Exposure	62.3%

Top 5 Positions (in alphabetical order)	16.9%
CSR	
Healthscope	
National Australia Bank	
Spark Infrastructure	
Westfield Group	

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