

Pengana Emerging Companies Fund

May 2010 Update



PENGANA
CAPITAL

Australian Equities - Small Caps

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Fund Performance

Net performance for periods ending May 31 2010 ¹							
	1 month	3 months	6 months	1 year	3 years p.a.	5 years p.a.	Since inception p.a. ²
Pengana Emerging Companies Fund	-7.6%	-1.3%	-0.9%	42.1%	-7.2%	14.2%	13.9%
S&P/ASX Small Industrials Acc Index³	-8.0%	-5.1%	-5.6%	22.0%	-16.6%	0.1%	0.4%
Outperformance	0.5%	3.8%	4.6%	20.2%	9.3%	14.1%	13.6%
S&P/ASX Small Ordinaries Acc Index	-8.2%	-1.9%	-5.7%	19.0%	-13.1%	4.7%	4.5%
Outperformance	0.6%	0.6%	4.8%	23.1%	5.8%	9.5%	9.4%

Fund Commentary

Global markets tanked in May due to fears over the European economies and signs of a slowdown in China. Global cyclical stocks were hardest hit, as was the \$A which is closely tied to commodity prices. The proposed increases in taxation in the resources sector added to nerves.

Over the month the fund fell 7.6%¹, which was less than the 8.2% fall in the Small Ordinaries Index and 8.0% fall in the Small Industrials Index. For the 12 months to May, the fund has returned 42.1%¹ which is 23.1%¹ above the Small Ordinaries Index and 20.2%¹ above the Small Industrials Index.

Global issues aside, there have been a number of profit warnings affecting our sector of late. The primary area of weakness relates to consumer spending, which we had highlighted as a risk in recent reports given rising interest rates and a lack of stimulus which aided last year's sales.

Somewhat lost in the noise of short term concerns was a dramatic uptick in corporate activity during May. We have seen six takeover offers tabled in smallcap industrial stocks (Ammtec, Boom Logistics, Dexion, Healthscope, Sigma Pharmaceuticals and Wattyl). This highlights the value seen by longer term investors (corporates and private equity), and also shows that funding channels are opening again for well structured deals. The lower \$A is also a benefit to overseas buyers of Australian listed companies.

Valuations have pulled back of late to quite cheap levels. The key question is how earnings will be affected by a tougher economic backdrop, if this transpires. We retain a relatively low exposure to stocks which require a strong economy to justify share prices, and are highly encouraged by the cheap valuations on many stocks which do not heavily rely on the economy to grow earnings.

In summary the situation in global economies remains fluid, hence taking a definitive view is fraught with risk. We are confident, however, that current valuations on the stocks we own show strong medium term upside even if economic challenges increase. The pull back in the market of late shows just how nervous investors are, and history shows the best opportunities often arise in times of collective fear.

¹ All performance figures are calculated net of fees and assume reinvestment of income distributions. Past performance is not a reliable indicator of future performance.

² Since November 2004

³ The Fund does not invest in resource stocks

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Key stock price moves

Key successes during May were MacMillan Shakespeare (+26%), Thorn Group (+7%), Resmed (+6%), Slater & Gordon (+2%), and Dominos Pizzas (+2%). Negative contributors included Kathmandu (-18%), Mineral Resources (-16%), Automotive Holdings (-14%), CSG Group (-12%), and REA Group (-12%).

Portfolio information

Top 10 Positions (in alphabetical order)	
CSG Group	Mineral Resources
IOOF	M2 Communications
Kathmandu	REA (realestate.com.au)
MacMillan Shakespeare	Slater & Gordon
Mac Services	Toxfree

Fund Description

The Pengana Emerging Companies Fund combines the skills of highly experienced small company investors (collectively 30 years experience) with a limited fund size and an objective of providing above market returns over the medium term. Our benchmark is the S&P/ASX Small Ordinaries Accumulation Index. The fund managers Steve Black and Ed Prendergast are part owners of the business and investors in the Fund, providing a strong incentive to perform. The Fund has strong research ratings from all major research houses and over the period since its inception has delivered returns well above benchmark.

Fund Features

Style	Bottom up stock picker	Management Fees	1.3325%
Benchmark	S&P/ASX Small Ordinaries Accumulation Index	Performance Fees	20.5% of the performance above the Benchmark
Investors	Open	Fund Raising	Maximum of 0.5% of the Benchmark capitalisation
Minimum Initial Investment Amount	A\$25,000 (direct)	FUM at Month End	A\$ 370m
Inception Date	1 November 2004	Application Price at Month End	A\$ 1.6933
Identification Code(s)	APIR PER0270AU ARSN 111 894 510	Redemption Price at Month End	A\$ 1.6831

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