

Pengana Australian Equities Core Fund September 2010 Update, by Rhett Kessler



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Fund Description

The Pengana Australian Equities Core Fund aims to provide investors with an annualised return of 12 to 15%¹ over the medium term via a concentrated core portfolio of principally listed Australian securities. The Fund is managed out of Sydney, Australia and uses fundamental research to evaluate investments capable of generating the target return over the medium term.

The Fund has released its Product Disclosure Statement (PDS) providing a more efficient access regime to investors including a lower Minimum Initial Investment and Daily Unit Pricing.

Fund Features

Application Price at Month End	A\$1.2190	Redemption Price at Month End	A\$1.2130
Style	Fundamental	FUM at Month End	A\$16.7m
Investors	Retail & Wholesale Clients	Management Fees	1.025% p.a. of NAV (including GST, net of RITC)
Benchmark	The average of the daily target Australian Cash Rate used by the RBA	Performance Fees (quarterly)	10.25% (including GST, net of RITC) of increase in net asset value subject to the Australian Cash Rate and High Water Mark
Inception Date	30 June 2008	Minimum Initial Investment	A\$20,000

Fund Commentary

Fund Performance (A\$, net of fees) ²													
	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	FYTD
2008/9	-1.0%	3.5%	-4.7%	-9.0%	-5.3	3.9%	0.2%	-1.4%	7.9%	4.4%	2.2%	3.7%	3.0%
2009/10	3.5%	6.1%	3.8%	1.2%	1.0%	2.5%	-3.6%	1.1%	3.6%	-0.2%	-4.0%	-2.5%	12.5%
2010/11	5.1%	1.1%	3.6%										10.0%

The Fund's return for September was a healthy 3.6%² after all fees and costs. By way of comparison the Australian All Ordinaries was up 5.0% for the month and the prevailing cash rate during September was 0.4%.

For the 27 months since inception the Fund has protected capital and provided investors with a satisfactory total annualised return of 11.4% versus the cash rate (4.2% annualised) and the negative market return generated by the Australian All Ordinaries (-1.7% annualised).

As at the 30th of September, the cash portion of the Fund's NTA stands at **18%**. Importantly the Fund's investment strategy remains focussed on companies with transparent and resilient business models, run by competent management and capable of generating satisfactory returns at the current prices.

Large positive contributors to the month's performance were McMillan Shakespeare, Westpac Bank, Seven Group Holdings, and Mermaid Marine. While there were no significant detractors, those holdings which registered minor negative contributions included NIB Holdings, Westfield Holdings and News Corporation. The Fund increased its holdings in Salmat, ANZ Bank and News Corporation. The Fund took advantage of an attractively priced secondary placement to acquire a new holding in Wide Bay Australia – a regional financial services company. The Fund disposed of its holding in Mitchell Communications following the take over bid by offshore media group Aegis. In addition the Fund trimmed its exposures to McMillan Shakespeare and Graincorp.

As at 30th September 2010 the top five holdings by value in the Fund were: Westpac Bank, McMillan Shakespeare, ANZ Bank, NIB Holdings, and News Corporation.

Net Returns to 30 th September 2010 ²			
	Pengana Core	Cash Rate	All Ordinaries
1 Month	3.6%	0.4%	5.0%
3 Months	10.0%	1.1%	8.7%
6 Months	2.7%	2.2%	-3.3%
1 Year	8.6%	4.0%	1.7%
2 years annualised	14.3%	3.9%	4.5%
Annualised return Inception	11.4%	4.2%	-1.7%

¹ This is not intended to be a forecast, but merely an indication of what the Fund aims to achieve over the medium to long term. The Fund may not be successful in meeting this objective. Returns are not guaranteed.

² Total return performance figures are derived from Managers' records and are shown after all fees and expenses, and assume reinvestment of distributions. Investments can go up and down. Past performance is not a reliable indicator of future performance. Inception date: 30 June 2008.

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Market Commentary

Market Review

Global equity markets bounced hard during September as investors focussed on the US being forced to extend the duration of the current remarkably low interest rate environment. The ASX All Ordinaries Accumulation Index finished up a healthy 5.0%. Interestingly, Incoming foreign investors were further rewarded (another 9%) due to the benefits of a rampant Australian Dollar. Industrials (+7%), Materials (+6%) and Utilities (+6%) were the strongest performing sectors while perennial underperformer Telcos (-4%) and REITS (-1%) were the only negative sectors.

The capitulation by investors who had been cynical of the underlying resilience in the Australian economy was probably a feature of this month. Both equity markets and the currency reflected a much stronger appetite for Australian "Risk" assets. The plethora of positive data included large trade surpluses (an unusual feature for Australia), ongoing robust employment statistics and improving retail sales.

Investment Outlook

The medium term economic outlook for OECD Group countries (appropriately grouped under the reference of "HICS" – Heavily Indebted Countries) remains subdued. However the robust GDP growth forecasts for the emerging economies (or "BRICs") including Brazil, Russia, India and China and most of South East Asia stands in sharp contrast. The ability of these countries to sustain regional growth without the larger developed economies (The much discussed "decoupling effect") represents a key investment variable for Australia. Concrete evidence of Australia's competitive advantage in providing significant quantities of high quality, low cost **coal** and **iron ore**, (with **wheat** potentially bolstering FY11) to these "growth markets" continues to be provided by the recent trade surpluses.

These positive factors are expected to support a strong domestic economy and enhance the virtuous circle of stable financial systems, low unemployment levels and above trend population growth (while not without exaggerating the imbalances of our two speed economy). **Importantly, the combination of the sharp increase in equity prices and the Australian Dollar has gone some way towards capturing the upside from these opportunities, highlighting the need for caution.**

Many market participants seem obsessed by whether the "market" is headed higher or lower. The Pengana Australian Equities Core Fund continues to focus on identifying companies with competent management and resilient business models that can take advantage of secular trends to generate significantly higher earnings and cash flows in the future, irrespective of whether the markets are higher or lower.

An example of this investment philosophy is represented by the Fund's holding in Seven Group Holdings. The company represents a diversified (both by business model and geographical exposure) group of assets that include exposure to: A) Media properties - the free-to-air broadcasting (Seven Network), Western Australian newspapers, domestic payTV and B) Caterpillar franchises in Western Australia and China. Importantly management has proven itself to be an astute manager of these businesses with a solid reputation for focussing on sustainable, growing after tax returns to shareholders.

Other examples of this can be found in several defensive companies with competent management, dominant market shares, pricing power and robust balance sheets. Lower share prices in a weak equity market provide more attractive entry points for the Fund which is focussing on after tax cash earnings yields.

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