

Pengana Emerging Companies Fund

October 2010 Update



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Australian Equities - Small Caps

CAPITAL

Fund Performance

Net performance for periods ending October 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	2.4%	12.2%	6.7%	16.4%	-5.6%	13.7%	15.6%
S&P/ASX Small Industrials Acc Index ³	2.0%	9.6%	0.4%	1.9%	-14.5%	-0.8%	1.8%
Outperformance	0.4%	2.6%	6.3%	14.4%	8.9%	14.5%	13.8%
S&P/ASX Small Ordinaries Acc Index	3.3%	14.7%	6.7%	11.5%	-10.1%	4.9%	6.9%
Outperformance	-0.9%	-2.5%	0.0%	4.9%	4.5%	8.8%	8.7%

Fund Commentary

October marked the sixth year of the fund. Since inception we have delivered a return after all fees of 15.6% p/a¹, which is 13.8% p/a above the Small Industrials Index^{1,3} and 8.7% p/a above the Small Ordinaries Index¹. The extreme market conditions over the six years have proven challenging, and we are pleased with these performance figures, and their consistency over time.

During the month our fund rose 2.4%¹ which exceeded the industrial benchmark, however it fell behind the Small Ordinaries due to a very strong resources sector. Through October, markets consolidated the gains from September, primarily lead by resources. The US Federal Reserve's massive quantitative easing measures buoyed the riskier sectors of the market as investors saw the potential for asset inflation due to increased money supply.

We have written a lot recently about the likelihood of increased corporate activity following the 15+ takeover offers made in the small industrial sector since May. This continued in October with an offer for Mac Services (one of our top 10 holdings) and offers for larger stocks such as the ASX and Perpetual. Clearly longer term investors are seeing value through the volatility which is not being recognised by shorter term investors.

The domestic economy remains sound with unemployment falling, and inflation in check. We see strong upside in corporate spending, especially in the mining sector which has moved strongly into expansion phase again. Infrastructure spending also looks to increase with State governments looking to boost capacity to cope with a growing population.

Conversely, the retail sector is tough given the lack of government handouts, and rising interest rates. Most discretionary retailers are cautious, and their share prices have underperformed this calendar year. This has created selective opportunities for us to buy into stocks such as Fantastic Furniture which we believe will rally strongly if sales stabilise.

Overall the industrial sector of the Smallcap market remains highly prospective for disciplined stock pickers. The volatility in markets shows just how short term most investors are. Typically in times of volatility, the true value of quality stocks goes unnoticed which is exactly the inefficiency we hope to capitalise on over the medium term.

Key stock price moves

Key successes during October were **DKN** (+37%), **Mastermyne** (+20%), **Mac Services** (+18%), **Slater & Gordon** (+14%), and **M2 Telecommunications** (+12%). Detractors included **REA Group** (-10%), **Mineral Resources** (-6%), **Kathmandu** (-12%) and **Transfield Services** (-4%).

¹ Net performance figures are derived from Manager's records and are shown after all fees and expenses, and assume reinvestment of distributions. Past performance is not a reliable indicator of future performance. The value of investments can go up and down.

² Since November 2004

³ The fund does not invest in resource stocks.

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Portfolio information

Top 10 Positions (in alphabetical order)	
CSG Group	M2 Telecommunications
IOOF	Ramsay Healthcare
MacMillan Shakespeare	REA (realestate.com.au)
Mac Services	Resmed
Mineral Resources	Slater & Gordon

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\$ 468m
Inception Date	1 November 2004	Application Price at Month End	A\$ 1.9446
Identification Code(s)	APIR PER0270AU ARSN 111 894 510	Redemption Price at Month End	A\$ 1.9329

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