

Pengana Australian Equities Core Fund

April 2011 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.

Since inception in June 2008 the Fund has consistently protected capital and provided investors with a robust total annualised return of 12.0% versus the cash rate (4.2% annualised) and the flat market return generated by the Australian All Ordinaries (1.3% annualised). **In addition the Fund's twelve month return of 11.3% in a difficult environment (Cash rate : 4.2% and Australian All Ords : 5.4%) is worth noting.**

Fund Features

Application Price at Month End	A\$1.3099	Redemption Price at Month End	A\$1.3034
Style	Fundamental	Current FUM Fund/Strategy	A\$39m / A\$60m
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

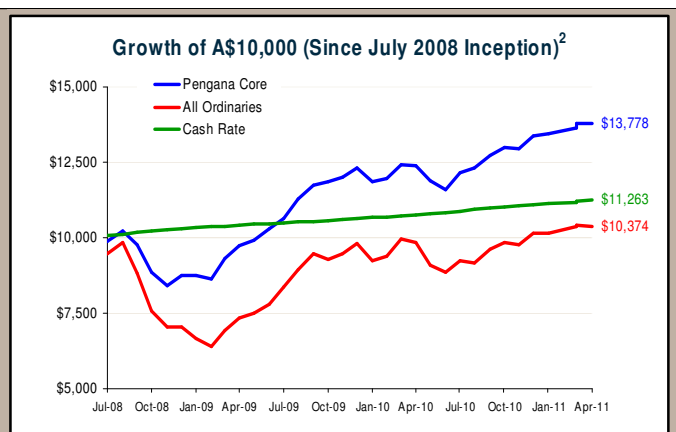
	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	FYTD
2008/9	-1.0%	3.5%	-4.7%	-9.0%	-5.3	3.9%	0.2%	-1.4%	7.9%	4.4%	2.2%	3.7%	4.3%
2009/10	3.5%	6.1%	3.8%	1.2%	1.0%	2.5%	-3.6%	1.1%	3.6%	-0.2%	-4.0%	-2.5%	12.5%
2010/11	5.1%	1.1%	3.6%	1.8%	-0.1%	3.0%	0.7%	1.5%	1.0%	0.0%			18.9%

The Fund generated a flat return of 0%² during April, net all fees and costs. By way of comparison the Australian All Ordinaries was down -0.6% for the month and the prevailing cash rate stood at 0.4% during the same period.

As at April 30th, the cash portion of the Fund's NTA stood at **19%**. The top five holdings by value are: **DUET, NIB Holdings, CBA, Seven Group, and ANZ Bank**. Large positive contributors to the past month's performance included NIB Holdings, Australian Power, CBA, Telstra and DUET. The detractors included CSG Group, CSL and McMillan Shakespeare. The Fund acquired additional exposure to the banking sector through a new holding in NAB. The Fund also acquired a stake in Symex - a manufacturer and distributor of consumer products. The Fund disposed of its holdings in Westfield Holdings and David Jones.

Net Returns to 30th April 2011²

	Pengana Core	Cash Rate	All Ords	Std Dev	Sharpe Ratio
1 Month	0.0%	0.4%	-0.6%	N/A	N/A
3 Months	2.5%	1.1%	2.3%	N/A	N/A
6 Months	6.2%	2.3%	5.5%	N/A	N/A
1 Year	11.3%	4.6%	5.4%	8.6%	0.78
Annualised Since Inception	12.0%	4.2%	1.3%	12.1%	0.64



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.

Pengana Capital Ltd (ABN 30 103 800 568, Australian financial services license number 226566) is the issuer of units in the Pengana Australian Equities Core Fund (ARSN 146 346 929) (the "Fund"). A product disclosure statement for the Fund is available and can be obtained from our distribution team. A person should obtain a copy of the product disclosure statement and should consider the product disclosure statement carefully before deciding whether to acquire, or to continue to hold, or making any other decision in respect of, the units in the Fund. This report was prepared by Pengana Capital Ltd and does not contain any investment recommendation or investment advice. This report has been prepared without taking account of any person's objectives, financial situation or needs. Therefore, before acting on any information contained within this report a person should consider the appropriateness of the information, having regard to their objectives, financial situation and needs. Neither Pengana Capital Ltd nor its related entities, directors or officers guarantees the performance of, or the repayment of capital or income invested in, the Fund.

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Market Commentary

Market Review

One of the main features during April was the strength of the Australian Dollar which closed at an exchange rate of A\$/US\$1.09. The ASX All Ordinaries Accumulation Index finished the month down -0.6% as investors began to balk at the implied cost of A\$ denominated earnings against a backdrop of an increasingly cautious domestic consumer. Consequently most global markets enjoyed broadly positive returns for the month but domestically the defensive Telecoms (+3.2%), Utilities (+2.4%) and Financials (+1.9%) sectors generated the best returns. The more volatile Industrials (-3.8%), Consumer Discretionary (-2.4%) and Energy sectors (-2.2%) were the largest decliners.

Investment Outlook

As conservative investors focussed on business models generating resilient after tax earnings, we constantly assess and reassess our investment theses, in particular the reliability of our fundamental assumptions. One essential building block to any investment thesis is the quantum of the "Risk Free Rate" (RFR). The current uncertainty (and paradox) surrounding the yield on US Treasury Bonds, (the RFR proxy for a whole generation of investors) is forcing a re-think of many global portfolios. In our view, investment returns from most asset classes are being shaped by the current currency war (or "race to the bottom") between the US, Europe and Japan. With each of them attempting to monetise their debt and make their export sector more competitive globally, many producers are being buffeted by the volatility in US\$ commodity prices.

Importantly several Asian economies are being tested as their pegged currencies create a difficult environment of high inflation and negative real interest rates. While we continue to be impressed by the ability of the Chinese authorities to manage these complex stresses, the margin for error continues to shrink. In a nutshell, they are being asked to navigate a very narrow path between maintaining the Yuan at an increasingly unrealistic level (to sustain employment levels in critical export sectors) or allowing the currency to appreciate providing some relief from the inflationary impact of sharply higher soft and hard commodity prices for their citizens.

Australian exports remain well placed to benefit from a stronger Chinese currency although we question whether current record levels of demand can be maintained. Australia certainly continues to be a major beneficiary of its fortunate position (both geologically and geographically) as a low cost **coal** and **iron ore** supplier. However the "China Dividend" continues to put enormous pressure on the domestic economy through higher interest rates, a robust A\$ and the negative consequences for tourism, education and retail sectors.

The Fund remains well positioned to participate in the medium term structural wealth creation spurred by a growing and gainfully-employed population. However, we are becoming increasingly concerned about the implications of a domestic economy that is dependent on the mining sector operating at a high capacity level. The resulting strong A\$ with a very high cost-of-living, distinguish us from comparable economies. We are being forced to question whether current rent, labour and property prices are sustainable and how much risk they represent for Australian corporate earnings.

Fund managers allocate capital to business managers who are expected to generate returns at a required rate. In selecting investments we not only evaluate the company's business models, but more importantly we take a view on the capabilities of the management teams to whom we have delegated this task. **One such investment that your fund has made is in NAB. The bold marketing initiatives adopted by management in differentiating its retail offering appears to be generating profitable incremental market share. These moves, coupled to the largest and resilient business bank in Australia, offer a good value entry point to the domestic banking oligopoly.**

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.

Examples of these 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 focussed on after-tax cash earnings yields.

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