

Pengana Australian Equities Core Fund

October 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.

For the 12 months ended 31st October 2011, the Fund has protected capital and provided investors with a positive return of 5.2%.² **Over the 3 year period, the Fund has generated a robust return of 15.5% p.a.², significantly higher than the Reserve Bank cash rate of 4.1% p.a. over the same period.** This is particularly pleasing given the very difficult investment environment as evidenced by the Australian All Ordinaries Accumulation Index's (the share market's) return of 7.6% p.a.

Fund Features

Application Price at Month End	A\$1.2664	Redemption Price at Month End	A\$1.2601
Style	Fundamental	Current FUM Fund/Strategy	A\$42m / A\$63m
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 the increase in net asset value subject to the Australian Cash Rate & High Water Mark
Inception Date	30 June 2008	Minimum Initial Investment	A\$20,000

Fund Commentary

Fund Performance (A\$, net of fees)²

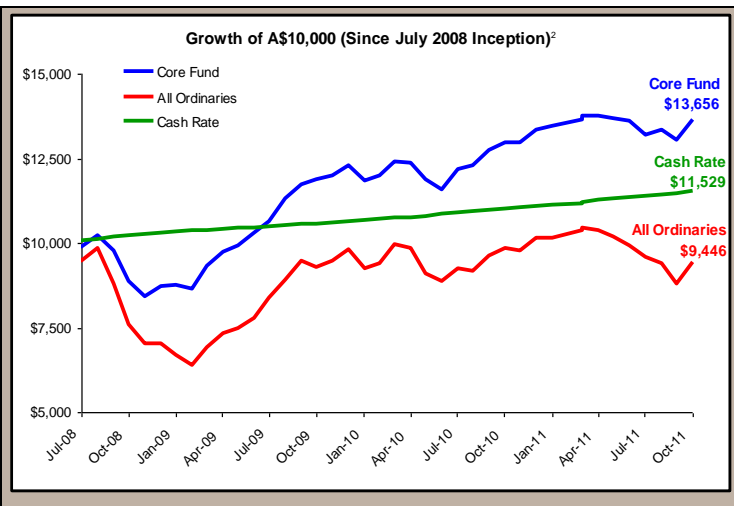
	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	FYTD
2008/9	-1.0%	3.5%	-4.7%	-9.0%	-5.3	3.9%	0.2%	-1.4%	7.9%	4.4%	2.2%	3.7%	3.0%
2009/10	3.5%	6.1%	3.8%	1.2%	1.0%	2.5%	-3.6%	1.1%	3.6%	-0.2%	-4.0%	-2.5%	12.5%
2010/11	5.1%	1.1%	3.6%	1.8%	-0.1%	3.0%	0.7%	1.5%	1.0%	0.0%	-0.8%	-0.5%	17.4%
2011/12	-3.1%	1.4%	-2.4%	4.7%									0.4%

The Fund generated a robust return of **4.7%**² for October, net of all fees and costs. By way of comparison the Australian All Ordinaries rebounded sharply to close up **7.2%** for the month and the prevailing cash rate returned at **0.4%**. As at October, 31st, cash (including notes and preference shares) represented **11%** of the fund. The top five holdings by value are: **DUET, NIB Holdings, NAB, McMillan Shakespeare and CBA.**

Large positive contributors to the month's performance included Seven West Media, NAB, NIB Holdings, McMillan Shakespeare, CBA and DUET. The largest detractors were Resmed, and Woolworths. Significant net acquisitions to existing holdings during October included Woolworths, Orica Preference Shares (less than 60 days to redemption), Emeco Holdings and Seven Group. The Fund lightened its holdings in News Corporation.

Net Returns to 31st October 2011²

	Pengana Core	Cash Rate	All Ords	Std Dev	Sharpe Ratio
1 Month	4.7%	0.4%	7.2%	N/A	N/A
3 Months	3.6%	1.3%	-1.6%	N/A	N/A
6 Months	-0.9%	2.5%	-8.9%	N/A	N/A
1 Year	5.2%	4.8%	-3.9%	7.4%	0.07
2 Years annualised	7.2%	4.5%	0.9%	8.7%	0.33
3 Years annualised	15.5%	4.1%	7.6%	10.2%	1.11
Annualised Return Since Inception²	9.8%	4.3%	-1.7%	11.8%	0.46



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

The domestic market (Australian All Ordinaries Accumulation Index) bounced sharply to finish October up 7.2%. In addition the A\$ rallied against the US\$ by 9%, providing offshore investors with very healthy boost to their Australian investment returns. Sectors reversed their respective trends established over the last 6 months with the Energy (12.3%), Financials (9.2%) and Materials (7.9%) sectors generating the largest monthly returns. The defensive Telecoms (-0.2%), Consumer Staples (0.3%) and Healthcare (0.9%) sectors were the weakest performers.

Global equity markets performed strongly during October as investors turned their attention to what could go right after a long period of only focussing on what could go wrong. Given the high levels of cash on the sidelines and the extremely low base for both valuations and investor sentiment, the levels of price volatility are expected to continue. In addition, as predicted in prior monthly commentaries, several sizable financial market participants have "confessed" to being on the wrong side of the recent volatile movements in market prices.

Investment Outlook

Professional investors face an interesting conundrum. From a macro perspective the impact of unsustainable sovereign debt levels in many important economies will limit economic growth for many years. Business confidence remains brittle as banks continue to be cautious lenders and consumers continue to exercise restraint in spending. Yet in spite of these negative operating conditions, there are many good businesses with competent management and robust balance sheets that continue to trade profitably on a sustainable basis. Importantly the share prices of many of these companies do not reflect their superior business models or attractive future cash flows. In our view, the current environment offers a significant opportunity to acquire high quality future after tax earnings streams at very attractive prices.

While two months ago many global investors appeared to have capitulated in the face of deteriorating European sovereign debt issues, October saw a sharp bounce as Greek debt holders take a 50 cents in the dollar haircut. Make no mistake, we remain very concerned about the outlook for global economic growth as high levels of unemployment continue to sap consumer confidence and defer any meaningful recovery in retail sales. Furthermore at a micro level, many consumer focused businesses are enduring a tough combination of subdued revenues, higher input costs and tighter lending conditions.

However, the recent broad based (and in our opinion – indiscriminate) sell-off by nervous investors has created many attractive investment opportunities for the Fund. We continue to be pleasantly surprised at the range of investment opportunities to acquire high quality companies with solid balance sheets, pricing power and largely economically insensitive business models.

The recent sell-off in Seven West Media share price is a good example of a structurally sound business with competent management offering compelling value due to irrational share price movements. At its low point, the company's shares offered investors the opportunity to invest in Australia's leading free to air network – Seven Network, Western Australian Newspapers, Pacifica Magazines and a 50% stake in Yahoo Australia, on a 22% fully franked (and in our view – sustainable) dividend yield. The Fund was able to take advantage of this opportunity to generate significant franking credits and healthy capital gains.

Contact Details

Pengana Capital Limited • Level 12, 167 Macquarie Street, Sydney, NSW 2000, Australia • T +61 2 8524 9900 • F +61 2 8524 9901
ABN 30 103 800 568, AFSL 226566

For further information, please visit our website at www.pengana.com or contact:

Private Clients:	Gale Ruttanaphon	+61 2 8524 9918	gale.ruttanaphon@pengana.com
	Tom Curtis	+61 2 8524 9986	tom.curtis@pengana.com
Advisors:	Damian Crowley	+61 2 8524 9970	damian.crowley@pengana.com
	Justin Brooks	+61 3 8663 7906	justin.brooks@pengana.com