



# Smaller companies, surprising opportunities

Challenger Smaller Companies Fund

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# Challenger Smaller Companies Fund

There are around 1,800 companies listed on the Australian Stock Exchange (ASX)<sup>^</sup>. The 100 largest companies, also known as large capitalisation companies (or 'large caps'), account for approximately 80% of the value of the entire Australian share market.

Compared to most large cap companies which tend to be very well researched, most small cap companies are not as well researched or understood by investors and as a result the market for investment in these companies is less 'efficient'. This creates a wide range of opportunities within the small cap universe for an experienced investment specialist to identify undervalued companies or companies with strong growth prospects that have not been fully understood or appreciated by the market.

**Market inefficiencies** are simply any factors that cause a company's share price to move away from its fundamental value, including:

- lack of perfect knowledge about a company;
- a lag between company announcements (e.g. revised company earnings and profit) and revaluations;
- investor sentiment, and
- other short-term influences that obscure a company's longer-term outlook.

The **Challenger Smaller Companies Fund** invests only in companies outside of the 100 largest companies listed on the ASX. While these smaller companies can include start up businesses and small operations, many are established operators and some are household names, like David Jones.

<sup>^</sup> Source: IRESS, as at 23 January 2007.

## Quality companies, not just good stocks

At Challenger, we believe that investing is more than just selecting good stocks – it's about buying quality companies. To find these companies our professional investment managers conduct in-depth research through visits and interviews with management. We also analyse a company's competitive environment, customers, suppliers and comparable overseas industries to determine trends and potential growth opportunities for local businesses.

Our aim is to find companies that can achieve significant share price growth over a three year investment timeframe. To achieve this we tend to stay away from the more trendy investments and stick to our guns, investing for the long term in high calibre companies.

## A concentrated portfolio

The Australian small companies universe contains about 1,700 investment opportunities. Instead of spreading the Fund's investments across a large number of stocks and achieving returns similar to the index, we take a 'high conviction' approach.

Our portfolio currently contains investments in about 25-45 companies – enough to ensure an appropriate level of diversification but not too many to take the kick out of our performance.

## Investment process



We continually monitor and review the companies in the Challenger Smaller Companies Fund to ensure the rationale behind each investment still holds true.

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## Portfolio construction and management summary

Market segment	Smaller companies
Universe	Securities outside the S&P/ASX 100
Benchmark	S&P/ASX Small Ordinaries Accumulation Index
Style	Bottom-up stock selection
Stock selection criteria	Investment decisions are based on qualitative and quantitative factors including fundamental research
Number of stocks	25-45
Investment timeframe	At least five years

To find out more about how investing in the Challenger Smaller Companies Fund can add value to your portfolio, contact your financial planner, visit our website **[www.challenger.com.au](http://www.challenger.com.au)** or call the Challenger Investor Services team on **13 35 66**.

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