



Atom Small Cap Fund May 2009 Report

Atom Small Cap Fund Before Fee Return History			
Period Ending	ASCF	Index*	Alpha
1 Month Return	8.9%	7.4%	1.5%
3 Month Return	32.0%	34.4%	-2.4%
6 Month Return	23.6%	24.5%	-0.9%
1 Year Return	-39.9%	-38.5%	-1.4%
Calendar Year Return	28.3%	19.6%	8.7%
Since Inception (1 Dec, 2007)	-30.8%	-33.1%	2.3%
* Small Ordinaries Accumulation Index			
Atom Small Cap Fund Unit Mid-Price	After Fees		\$0.5518
	Before Fees		\$0.5752
Stocks in Portfolio (#)			44
Fund Size (\$m)			8

INVESTMENT PHILOSOPHY & RISK

Whilst markets have been trending up they remain volatile. In particular there is a battle of wills regarding “defensives” and “cyclicals” as to which will outperform day to day.

We expect a modest rise in equity markets into late 2009, driven by a slowing in the rate of economic deterioration (and patches of improvement) and an investor willingness to look into 2010 – where economies should be improving albeit slowly and off a low base.

Its important for us to be honest with ourselves at all times – we are not certain that above picture is cast in stone. Exogenous shocks in the form of deterioration of European banking health or unemployment data in the USA could unsettle the recently awoken bulls and send them reeling back into their caves to hibernate for a few more months.

So, we have a binary outlook in the medium term – a short sharp correction down (less likely) or a modest gradual rise as things slowly improve (most likely).

Prudently at times of doubt coupled with high volatility we position the portfolio with somewhat of a balance between cyclical stocks (those which will run as the economy improves) and defensive stocks (those that will fall less if markets

deteriorate). In this way either outcome, if coupled with good stock picking, can achieve out performance of our benchmark index.

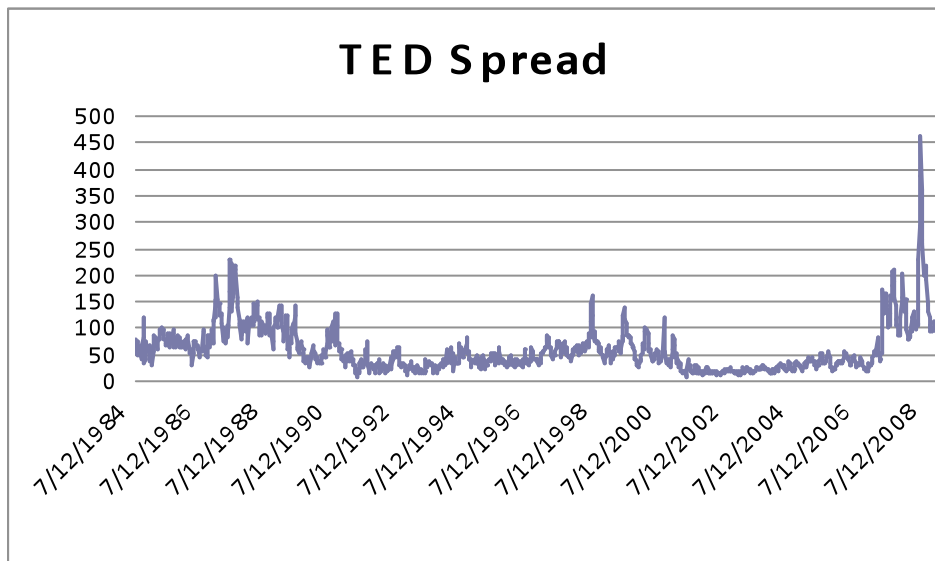
Again, we'll never change our core philosophy of searching through the large number of stocks outside the ASX Top 100 to find the small number of opportunities where we have high conviction of success.

MARKET OUTLOOK

We remain cautiously optimistic for Australian equities as we head into the end of 2009, with a continuing view that select small and mcirocap opportunities offer greater scope for outperformance than the ASX Top 100. They are simply on lower PER's and many have unique business models which are growing strongly.

The key, as always, is detailed research and stock selection.

With the bounce in equity markets since March 2009, investor sentiment has improved. Importantly it is being accompanied by improving credit markets and equity market balance sheets. The Ted spread has almost retraced its rise over the last 2 years – a very bullish sign that banks will soon begin to lend again.



Credit spreads are narrowing, in other words the risk premium that corporations must pay for debt is reducing making corporate bond issues more attractive (should bank debt not be available). Corporate bond issuance is rising as a result.

Equity Raisings have accelerated – indeed we can not recall a time when these were more frequent. Listed companies are shoring up their balance sheets and stock brokers are predicting total raisings to equate to over 7% of the value of the stock market. With each raising generally comes (a) an evaporation of concerns regarding debt refinancing, (b) an evaporation of a pending equity issue [obvious], and (c) the balance sheet strength to possibly engage in take

over activity. All of these things are conducive to a more favourable equity market outlook.

We must anticipate as these factors continue to improve, there will be a rush of debt driven acquisitions [our best guess is by the end of this year].

This is not to say we will return to the debt driven madness of 2007, but rather those corporations with strong underlying cash flows and modest debt levels will begin to seek out and acquire smaller opportunities which are trading on low PER multiples.

Because we operate in the small and microcap space Atom's portfolio may be a beneficiary of the takeover action that should logically appear – that is if bargain hunters do not push share prices of “value” stocks up higher in the next few months (which we expect).

On the commodities front we note continued gains in commodity prices (precious, energy and base metals) and a lower than expected cut to annually negotiated iron ore prices.

Whilst short term there is the possibility of a pull back on exogenous shock news, long term we remain bullish with developing world growth requiring metals and energy for it to be sustained. The past 18 months has dented the worlds ability to supply commodities should global growth accelerate, and mines, power stations, ports and railways lines are long lead time infrastructure.

We highlight the OECD's International Energy Agency report of 25 May 2009 titled *The Impact of the Financial and Economic Crisis on Global Energy Investment...*

“a real danger that sustained lower investment in supply in the coming months and years, could lead to a shortage of capacity and another spike in energy prices in several years time, when the economy is on the road to recovery. The faster the recovery, the more likely that such a scenario will happen.”

We have positioned the portfolio to benefit from projects that will fuel the future growth in demand for commodities. These are stocks in companies with long mine lives and low cost projects and many of which can be expanded as demand allows.

MARKET COMMENTARY

For the Month

The Fund outperformed its benchmark index by 1.5% during May 2009, being up 8.9% compared to the index at 7.4%.

The largest detractors to our portfolio were;

- LNC - 16% - Linc Energy disappointed the market with a delay in planned sale of peripheral coal assets.
- UXC - 15% - UXC suffers from skepticism regarding a forecast improvement in earnings during the current half.
- PST - 11% - Pearl Street fell on low volume. Its fundamentals remain strong.

The largest contributors to our portfolio were;

- CLQ + 75% - CleanTeq is awaiting news of a first go-ahead on its uranium extraction technology from Palladin Energy (PDN).
- TSM + 72% - Thinksmart is a financial intermediary between electronic retailers and small businesses with operations in Aust, NZ, UK and Europe. It does not take credit risk, and benefits from the trend away from asset purchase to asset renting.
- CGG +40% - Citadel announced development of an associated gold project adjacent to the large planned copper mine with start up within 12 months.

CASH HOLDINGS

Cash holdings at end of May 2009 were approximately 0.8%.

SECTOR EXPOSURE

The following table outlines the portfolio's exposure by sector compared to the Small Ordinaries Accumulation Index (it's benchmark).

Sector	Sub-Sector	Small Ords Index	Atom Small Cap Fund	Active position
Energy		15.2	15.6	0.4
Materials	Mining	23.8	23.5	-0.3
	Other	3.3	-	-3.3
Industrials	Capital Goods	7.5	5.6	-1.9
	Commercial Service & supplies	6.3	12.4	6.1
	Transport	2.0	1.0	-1.0
Consumer Discretionary	Other	2.3	0.9	-1.5
	Media	3.6	-	-3.6
	Retail	2.2	4.1	1.9
Consumer Staples		2.7	5.0	2.2
Health Care		7.9	6.2	-1.7
Financials	Other	5.9	10.8	5.0
	Property Trusts	5.9	2.5	-3.4
IT		3.2	7.2	4.0
Telcos		0.1	3.5	3.4
Utilities		8.1	1.0	-7.0
Total		100.0	99.2	-0.8

Macro Comments

- The portfolio has a balance between cyclical and defensive stocks (taking into account our belief that some stocks are mislabeled by the ASX in terms of their true nature).

TOP ATOM STOCKS

We are pleased to present the top 10 holdings of the Atom Small Cap Fund.

Atom Small Cap Fund Top 10 Holdings*			
Stock name	ASX Code	Weighting (%)	Style **
Mirabela Nickel #	MBN	6.2	Value
Industrea	IDL	4.9	Value
Nido Petroleum	NDO	4.7	Value
iSoft	ISF	4.2	Value
Citadel Resource Group	CGG	4.2	NPV
Neptune Marine Service	NMS	4.0	Value
CleanTeq	CLQ	3.9	Value
Tox Free Solutions	TOX	3.8	Value
Independence Group	IGO	3.7	Value
Entertainment Media & Telecoms	ETC	3.5	Value

* Weightings at 31/5/09.

** Style refers to the nature of the valuation technique that defines present and near term financial attributes. "Value" equates to low PER, high yield and earnings growth. "NPV" equates to no present profitability but prospects for large future cash flows.

- Comparisons with last month will show radical moves in stock weightings – these are almost entirely due to rapid share price increases of a select number of stocks and not high turnover within the fund.
- ISF – iSoft – is the renamed IBA – IBA Health.
- # This month we have reclassified MBN as a Value stock even though it is not presently producing cash. The nickel mine it is developing is expected to start production in September 2009 (delayed 2 months) and be profitable at current depressed nickel prices. Thus because we are primarily focused on 2010 earnings will reclassify MBN as a "value" stock because it is on a low PER.

MATERIAL CHANGES TO PORTFOLIO

We added a number of stocks to the portfolio during May 2009.

AAX – Ausenco

- Ausenco is a mining contractor, designing and constructing mining operations around the globe. Its share price has been hit hard over the last year, and the recent capital raising at a discount allowed us an opportunity to gain exposure.

TSM – Thinksmart

- Thinksmart acts as an intermediary between business consumers (B2B) of electronic products in a retail environment and financiers. TSM have long term agreements with retailers and financiers alike offering their services through JB Hi-Fi and Dick Smith in Australia and internationally in the UK, Spain and Italy. The model is mature in Australia with expansion plans into new jurisdictions funded out of internal cash flows. TSM trades on low single digit multiple, generates strong cash flows and has low levels of debt.

REX – Regional Express

- Regional Express is an airline focused on rural to city links, the majority of routes being monopolies. REX is trading on a low PER and has manageable debt. Impressively it is profitable at present times because it has a lower operating and capital cost structure stemming largely from a decision to avoid the increased cost associated with jet aircraft (as Virgin has done).

Airlines warrant special mention – this is the first time in our collective lives as analysts that any of us have bought an airline stock. As an industry and throughout decades the cumulative global destruction in shareholder value of the airline industry has been enormous. The industry is capital intensive and produces a commodity product (a seat on a flight). We have looked in detail at the relative cost (capital and operating) of REX verses both Virgin and Qantas to conclude it is robust even if the present circumstances continue and will benefit from any improvement in the economy. Our analysis of Virgin and Qantas showed higher capital and operating cost structures. Indeed if conditions continue as they are today we concluded Virgin will require a significant capital raising.

COMPANY VISITS

We conducted 43 meetings with companies during May 2009. Since inception 65% of meetings have been one on one in nature. We aim for 600 company visits pa with the present team.

The nature of our visits is tilting more towards repeat visits with companies we already know and away from visits with completely unknown companies. This is a function of Atom getting older and we would expect this trend to continue.

Thank you. We look forward to updating you next month.

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