Perennial Value Smaller Companies Trust

Monthly Report
31 December 2014

	Month	Quarter	FYTD	1 year	3 years	5 years	Since Inception^
	%	%	%	%	% p.a.	% p.a.	% p.a.
Perennial Value Smaller Companies Trust*	-1.6	-10.6	-7.5	-3.9	3.9	2.7	9.5
S&P/ASX Small Ordinaries Accum. Index	0.5	-3.9	-2.4	-3.8	0.6	-2.0	4.8
Value Added (Detracted)	**-2.1**	**-6.7**	**-5.1**	**-0.1**	**3.3**	**4.7**	**4.7**

*Net performance (including performance fee). ^Since inception: March 2002. Past performance is not a reliable indicator of future performance.

Perennial Value Smaller Companies Trust

The Trust aims to grow the value of your investment over the long term via a combination of capital growth by investing in a diversified portfolio of Australian shares predominantly outside the S&P/ASX 100 Index, and to provide a total return (after fees*) that exceeds the S&P/ASX Small Ordinaries Accumulation Index measured on a rolling three year basis.

Portfolio managers:
Grant Oshry and Andrew Smith

Risk profile:
High

Trust FUM (as at 31 December 2014):
AUD105.6 million

Income distribution frequency:
Half yearly

Minimum initial investment:
$25,000

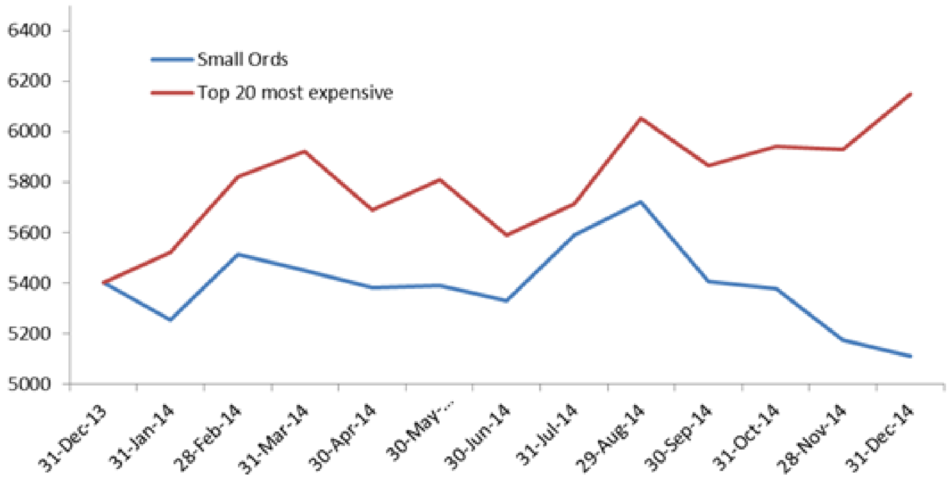
Trust inception date:
March 2002

APIR code:
IOF0214AU

- **The Australian share market, particularly the smaller end remains divided, with expensive momentum stocks continuing to outperform.**
- **The Trust trades on an FY15 P/E multiple of 12.5x, being a 22% discount to the benchmark, which we feel offers good value**
- **The best attributor during the month was gold producer Regis Resources (up 34.0%).**

The benchmark S&P/ASX Small Ordinaries Accumulation Index gained 0.5% during December. The Perennial Value Smaller Companies Trust (the Trust) declined 1.6% after all fees, thereby underperforming by a net 2.1%.

The Australian share market, particularly the smaller end remains divided, with expensive momentum stocks continuing to outperform. This is evidenced by the chart below which compares the strong outperformance of the top 20 most expensive Small Ord constituents versus the benchmark Small Ords during CY14.



Source: Goldman Sachs, December 2014

While the difference in total returns during CY14 is 19.2%, the divergence became more pronounced towards the end of the year and in particular December. These 20 index-heavy small caps trade on a 1-year forward P/E multiple of 21x-43x based on IBES consensus data. We regard this as expensive and thus do not own these in the Trust, remaining true to style. The strong performance of these stocks versus better value names in the portfolio has impacted our relative performance recently.

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December saw further slides in commodity prices, including the price of oil, which has had a significant impact on the prices of energy stocks. Global markets were softer, with the S&P500 (down 0.4%), FTSE (down 2.3%), Euro Stoxx 50 (down 3.2%) and Nikkei 225 (down 0.1%) all weaker. However, there was further evidence that global growth is improving. In particular, the data for the US was positive, with the revised Q3 GDP data showing the firmest rate of growth since 2003 and non-farm payrolls growing 321,000, well above expectations. In other regions, key German economic data improved, there were positive signs that Japan's economy is emerging from recession in the current quarter and China's data was consistent with growth at close to 7% in Q4, although a key manufacturing PMI dropped below 50. Global inflation continued to fall, suggesting a prolonged period of low interest rates.

In Australia, GDP growth was unexpectedly weak in the September quarter, with real disposable income falling again, however, the partial data for the fourth quarter pointed to improvement. Retail sales for October were soft, albeit better than expected and home building approvals boomed, as did employment for November. The jobless rate, however, rose to a new 12-year high of 6.3%, and business and consumer sentiment fell, with the mid-year economic update revealing further deterioration in the budget deficit, largely due to lower commodity prices. The RBA left interest rates unchanged at 2.5% and the AUD continued to fall, reaching a four-year low of 81 US cents.

The strongest performing sectors were Financials ex Property Trust (up 1.9%) and Materials (up 1.5%). The weakest sector was Energy (down 16.8%), followed by Utilities (down 14.5%).

The best attributor during the month was gold producer Regis Resources (up 34.0%) following stability in the gold price around US$1200, but a stronger $A gold price. Whitehaven Coal (up 12.9%) announced its first coal was being railed from its Maules Creek mine to the port at Newcastle three months ahead of schedule and below budget. This places the company in a good position to achieve better refinancing terms and covenants on its debt with mine development risk no longer significant and Maules Creek now generating cash flow.

Smash repair chain AMA Group (up 17.7%) announced their expansion into the Queensland market by acquiring a well-established player. This is in line with AMA's stated strategy and this transaction is also earnings accretive.

Detractors included US shale oil producer Sundance Energy (down 25.0%), largely attributable to the fall in the oil price as mentioned above. In light of this, the company announced that it has modified its 2015 capital programme to be funded from operating cash flow. It is also worth noting that the company has a sound balance sheet with net debt/EBITDA of 0.9x, which the Board intends to preserve following the announcement that the company will not be making any acquisitions. It is worth noting that this company's operating break-even production cost in the September 2014 quarter was US$20.40/barrel of oil equivalent (BOE) versus WTI's current oil price of US$54/BOE.

Austex Oil (down 19.4%) was sold off with the weaker oil price despite the company having 80% of its oil hedged above US$80BOE for the next two years and a balance sheet that is in a net cash position. It was pleasing to see that directors were purchasing shares on market during the month.

In terms of portfolio activity, we reduced our position in Regis Resources given the share price rally. We increased our exposure in medical equipment provider Life Healthcare, commercial property owner GDI Property Group, general insurer Tower and specialty retailer Super Retail which has exposure to the auto, leisure and sports markets.

Unitholders can look forward to a distribution for the half-year ended 31 December 2014 of 1.01CPU (paid in early January 2015), which represents a 12.0% increase on the prior corresponding period .

At month end, stock numbers were 54 and cash was 4.0%.

Asset Allocation

Sector	Trust weight %	Index weight %
Energy	9.2	5.1
Materials	9.3	14.5
Industrials	18.3	15.1
Consumer Discretionary	28.1	24.5
Consumer Staples	0.0	4.2
Health Care	1.5	6.6
Financials-x-Real Estate	10.2	7.9
Real Estate	13.3	11.4
Information Technology	3.2	4.8
Telecommunication Services	1.7	5.2
Utilities	1.3	0.7
Other	3.9	-

Rounding accounts for small +/- from 100%.

For all other enquiries please contact us on 1300 730 032 or visit www.perennial.net.au.

Signatory of:

PRI Principles for Responsible Investment