Perennial Value Smaller Companies Trust

Quarterly Report as at 31 December 2012

	3 Months %	1 Year %	3 Years % p.a.	5 Years % p.a.	Since Inception^ % p.a.
Perennial Value Smaller Companies Trust+	4.4	21.3	7.2	3.0	12.2
S&P/ASX Small Ordinaries Accum. Index	2.0	6.6	-1.8	-6.9	6.2
Value Added (Detracted)	**2.4**	**14.7**	**9.0**	**9.9**	**6.0**

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

- The Trust outperformed the Index return by 2.4%.
- Sector performance largely favoured the defensives with the best performers including financials (up 19.1%), consumer staples (up 16.1%) and property trusts (up 11.5%).
- STW Communications was added to the Trust during the quarter.

The December quarter was dominated by companies holding their annual general meetings, which was skewed towards earnings' downgrades given the sluggish domestic economy. International politics dominated global headlines and sentiment, particularly with US fiscal cliff negotiations (which were only resolved post-quarter end), while both China and Japan saw leadership changes in their respective governments.

The smaller end of the Australian equity market responded well with the S&P/ASX Small Ordinaries Accumulation Index (the Index) up 2.0% for the quarter. The Perennial Value Smaller Companies Trust (the Trust) finished the quarter up 4.4% net of all fees, thereby outperforming the Index return by 2.4%.

For 2012 calendar year, the Trust's net return was 21.3%, thereby outperforming the Index return, which gained 6.6%, by a healthy 14.7%.

Domestically, the Reserve Bank of Australia cut the cash rate by 0.5% over the quarter to 3.0% citing that a softening labour market and peaking mining capex gave scope for easing. Interest rates have now been cut by 1.75% since November 2011, which will hopefully provide further support to the Australian economy going forward. The unemployment rate was up by 0.1% to 5.2%. The Australian dollar was unchanged at USD1.04.

Sector performance largely favoured the defensives with the best performers including financials (up 19.1%), consumer staples (up 16.1%) and property trusts (up 11.5%). The weaker sectors were healthcare (down 9.0%), materials (down 8.3%) and information technology (down 7.2%).

Perennial Value Smaller Companies Trust Facts:

The Trust aims to grow the value of your investment over the long term via a combination of capital growth and tax effective income 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

Trust FUM (as at 31/12/12):
AUD114.9 million

Team FUM (as at 31/12/12):
AUD7.4 billion

Trust Inception date:
March 2002

Risk Profile:
High

Income Distribution Frequency:
Half yearly

Minimum Initial Investment:
$25,000

APIR code:
IOF0214AU

*Excluding performance fees.

The best performing stock in the Trust was Horizon Oil (up 43.3%) which benefited from a sizeable reserve upgrade at its New Zealand assets coupled with a significant increase in forecast production from its assets in Papua New Guinea.

Engineering firm Clough (up 32.9%) announced a host of new contract wins in addition to a material earnings upgrade late in the quarter. Given Clough is the largest active position in the Trust, we visited the company in Perth in mid-November for the fourth time this calendar year (which is in addition to eight other points of contact we had with management during 2012) to receive an update. Clough also benefited from its equity stake in mining services contractor Forge Group (up 25.1%), which also announced an earnings upgrade followed by a contract win from BHP Billiton to develop its Yarnima, WA power station.

Other stocks which contributed to the Trust's outperformance included Henderson Group (up 22.8%), Whitehaven Coal (up 22.0%), driller Swick Mining (up 19.6%), Amcom Telecommunications (up 18.7%) and TPG Telecom (up 17.9%).

Stocks which detracted from performance over the quarter included Redflex (down 24.9%) after it was revealed one of its employees paid for a hotel room for an employee of the City of Chicago, which is one of Redflex's material clients. This inappropriate action is being investigated by the Chicago Board of Ethics to determine if any further action is required, the outcome of which could put at risk the lucrative red light contract Redflex has had with the city since 2003. These revelations are concerning and we have subsequently discussed with management the circumstances surrounding this payment. While it appears to be an isolated incident (and further safeguards are now in place) it remains something we will monitor closely going forward. After the announcement we did reduce our holding (at an average price of $1.78 (versus quarter end closing price of $1.51), however the current price more than factors in the potential negative impact from the loss of the Chicago contract.

FKP Property (down 35.4%) conducted a discounted entitlement issue to provide more balance sheet flexibility. This stock has also underperformed despite recent positive asset sale announcements, which were within 10% of their net tangible asset value (NTA), thereby asserting the steep 70% discount that this stock currently trades at. Should this trend of asset sales continue, coupled with an improved residential housing market driven by lower borrowing rates, we are of the view that this discount to NTA will start to close.

Northern Iron (down 26.8%) also detracted from performance after announcing that neither of the two interested parties that were granted due diligence were to providing a margin of safety given its higher level of debt.

We remain alert to environmental, social and corporate governance (ESG) issues in the Trust. During the quarter, we added toy and content distributor Funtastic to the Trust. At an average entry price of 21 cents, this stock trades at a significant discount to the Small Industrials Index and profitability under the new management team has improved with dividends flagged as resuming in FY13, thereby placing this stock on an attractive yield. During our analysis, we ascertained that

in a position to lodge a formal offer by the company imposed deadline. While both parties have left open the possibility of renewed interest at a later time, the lack of a formal bid clearly disappointed the market. We used the weakness to add to our position given an attractive valuation and indications that costs will continue to come down next year.

In terms of Trust activity, following the collapse in the iron ore price (bottomed in September around $87 per tonne), and given we were are of the view that this commodity had been oversold on concerns of China slowing down, we added to our positions in Mount Gibson and Northern Iron in addition to adding Mineral Resources and BC Iron. The purchases allowed us to meet our objective to give the Trust a meaningful exposure to this commodity. Aside from Northern Iron (for reasons mentioned above), each of these stocks rose between 14% and 21%, benefiting from iron ore's price rise of 47% during the quarter.

We exited our profitable holdings in NIB Holdings, Technology One, Abacus Property Group and Mermaid Marine all on valuation grounds. Following strong share price appreciation, profits were taken in each of Amcom Telecom, TPG Telecom, Tox Free Solutions, Oroton, Forge, Clough and Horizon Oil. Proceeds were used to increase our exposures in Whitehaven Coal, SMS Management & Technology and Mount Gibson.

We added STW Communications to the Trust. This media company has a growing presence in digital advertising and the agency nature of its business means it faces less structural issues than traditional print and TV media. We believe it offers a lower risk exposure to a potential recovery in the advertising market, while rewarding investors with a higher dividend yield.

After reducing our exposure in Tox Free Solutions as mentioned above, we introduced Transpacific Industries to the Trust, which at an average cost of 68 cents (quarter end price 78 cents), placed the stock on a cheaper EV/EBIT multiple than its competitor in addition

Funtastic uses its best endeavours through contract negotiations to ensure that all of its products are manufactured in accordance with local and internationally accepted labour, environmental and employment laws. The company is working to ensure that manufacturing occurs under working conditions that meet legal standards and without the use of child, forced or prison labour.

At quarter end, stock numbers stood at 57 with cash at 3.5%.

Asset Allocation as at 31 December 2012

Asset Class	Trust Weight %	Index Weight %
Energy	20.0%	9.5%
Materials	15.5%	26.7%
Industrials	20.8%	22.7%
Consumer Discretionary	16.8%	15.6%
Consumer Staples	0.0%	1.4%
Health Care	0.0%	4.2%
Financials-x-Real Estate	4.1%	6.7%
Real Estate	2.7%	6.5%
Information Technology	6.9%	1.8%
Telecommunication Services	3.2%	3.6%
Utilities	1.1%	1.4%
Other	8.8%	-

Rounding accounts for small +/- from 100%.