PERENNIAL VALUE MANAGEMENT

Perennial Value Smaller Companies Trust

Monthly Report
29 February 2016

	Month	Quarter	FYTD	1 year	3 years	5 years	Since Inception^
	%	%	%	%	% p.a.	% p.a.	% p.a.
Perennial Value Smaller Companies Trust*	-1.0	-6.3	-2.2	-4.2	-2.5	-0.8	9.0
S&P/ASX Small Ordinaries Accum. Index	0.9	-0.5	2.5	-3.6	-1.4	-3.2	4.8
Value Added (Detracted)	**-1.9**	**-5.8**	**-4.7**	**-0.6**	**-1.1**	**2.4**	**4.2**

*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 29 February 2016):
AUD $110 million

Income distribution frequency:
Half yearly

Minimum initial investment:
$25,000

Trust inception date:
March 2002

APIR code:
IOF0214AU

- **February reporting season reflected an improving east coast economy overall, despite volatile share price reactions.**
- **Resources, particularly gold and iron ore, drove the Index higher, outperforming industrials.**
- **The Index finished up 0.9%.**

Trust performance

February was a volatile month globally, exacerbated domestically with companies reporting their interim results. Having been down for most of the month, the S&P/ASX Small Ordinaries Index (the Index) ended up 0.9%. The Perennial Value Small Companies Trust (the Trust) was down 1.0%, underperforming by 1.9% net of all fees.

The Index outperformed the broader market, largely due to strength in the resources and energy sectors. Whilst the Trust benefitted from a number of holdings exposed to these sectors, this was more than offset, however, by the strong performance of a range of non-held stocks, the large majority of which we cannot justify holding on valuation grounds. For example, index-heavy Syrah Resources (up 16.0%), does not pass our value process as it has no earnings given it is yet to commence producing graphite from its asset based in Mozambique, to which we assign a higher country-risk premium.

The key commodities driving resources were gold and iron ore. Whilst the Trust does have some gold exposure, we are underweight this sector as its value implies a gold price significantly higher than the spot US Dollar gold price. The second largest benchmark constituent, Northern Star (up 31.8%) is not held in the Trust given its valuation is incongruent with its short mine life. Our preferred holding is Independence Group (up 16.9%) given the attractive attributes and valuation of its Tropicana gold mine in Western Australia.

The Trust benefitted from its energy holding in Sino Gas (up 63.6%), but this was partially offset by Sundance Energy (down 36.7%), which lagged the sector as the market awaits a deleveraging transaction. We view a transaction as being increasingly likely as the oil price increases and we expect a material re-rating upon this event.

Our holdings in nickel producer Panoramic Resources (up 28.0%) and copper producer Sandfire Resources (up 13.8%) both rallied on firmer nickel and copper prices respectively. However, some of this shine was offset by weakness in Hillgrove Resources (down 30.0%) as this company continues to progress through a period of high material movement and modest cash generation as the final cut-back of its open pit descends towards higher grade ore. Hillgrove should begin to intersect higher grade material from the June quarter, at which point cash generation will improve.

Breville Group (up 25.3%) was the best industrial performer during the month. The stock was priced for a downgrade, following a weak result from competitor Sunbeam in late January. While Breville's domestic operational performance was subdued, their North American and European regions delivered strong interim results. The new Chief Executive Officer also elaborated on the company's plans to gain more global market share which resonated well with the market.

Source: Portfolio Manager Grant Oshry in Macys Union Square, San Francisco

APN News & Media (up 15.5%) reported a good result in their core radio division and signalled to the market that they are looking to divest their regional publishing business, which has been weighing on the share price. Gaming systems provider Intecq Limited (formerly eBet Group) (up 16.6%) delivered a very strong interim result, highlighting the strength of their business model that now derives 70.0% of its revenue from recurring sources.

Other strong performers during the month included energy consulting business Energy Action (up 24.4%), retirement owner and operator Aveo Group (up 6.7%), insurance broker Steadfast (up 13.7%) and furniture retailer Fantastic Holdings (up 10.3%).

The key industrial detractor was medical devices distributor Lifehealthcare Group (down 47.2%) following an interim result which missed consensus earnings by 10.0%. This was partly attributable by costs which are of a non-recurring nature. Consquently we feel the sell-off was overdone and we used the share price weakness to add to our position, and we are pleased to see the directors do the same.

Matrix Composite and Engineering (down 23.9%) declined following the cancellation of an order by a large customer. Murray Goulburn (down 21.0%) guided to a full year number slightly below the bottom end of their guidance given the pressure they face from a weaker dairy price. Super Retail Group (down 20.1%) reported a result that reflected strength in their core Auto and Sports businesses, which combined now account for 87% of Group earnings. However, it was a weaker than expected Leisure segment that led to its sharp selloff, given the market's impatience with this division's turnaround.

Trust Activity

In terms of Trust activity, after exiting Myer last November at a higher price we re-established a position during the month at an average price of $1.01 (month-end closing price $1.15). This was following positive post-Christmas feedback from suppliers and competitors coupled with an encouraging department store sales release from the Australian Bureau of Statistics for December 2015.

The Trust ended the month with 52 stocks and cash of 2.4%.

Outlook

In light of the de-rating of a number of companies during February's reporting season, we are seeing new investment opportunities emerge.

In the media sector, we are encouraged by the proposed media reforms that appear to be supported by the cabinet. Should these changes get through the Senate, we are of the view that they will lead to an increase in Mergers & Acquisitions. The Trust stands to be a beneficiary given its overweight exposure to this sector via our holdings in APN News & Media, Prime TV and Southern Cross.

As always, our focus will continue to be on investing in quality companies which are offering attractive valuations.

Asset Allocation

Sector	Trust weight %	Index weight %
Energy	3.3	2.5
Materials	7.3	16.8
Industrials	9.1	10.8
Consumer Discretionary	40.1	22.1
Consumer Staples	4.4	7.9
Health Care	4.3	7.2
Financials-x-Real Estate	10.7	8.0
Real Estate	11.5	12.7
Information Technology	4.0	6.7
Telecommunication Services	1.5	4.6
Utilities	1.3	0.7
Cash & Other	2.4	-

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