PERENNIAL VALUE MANAGEMENT

Perennial Value Smaller Companies Trust

Monthly Report
31 May 2017

	Month	Quarter	FYTD	1 year	3 years	5 years	Since Inception^
	%	%	%	%	% p.a.	% p.a.	% p.a.
Perennial Value Smaller Companies Trust*	0.4	-1.3	12.7	10.7	5.0	5.7	9.7
S&P/ASX Small Ordinaries Accum. Index	-2.1	0.3	4.9	3.5	6.0	4.2	5.5
Value Added (Detracted)	**2.5**	**-1.6**	**7.8**	**7.2**	**-1.0**	**1.5**	**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 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

Risk profile
High

Trust FUM
AUD $107 million

Distribution frequency
Half yearly

Minimum initial investment
$25,000

Trust inception date
March 2002

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- **The Perennial Value Smaller Companies Trust (the Trust) finished the month up 0.4% (net of fees) outperforming the S&P/ASX Small Ordinaries Accumulation Index (the Index) by 2.5%.**
- **Financial year to date, the Trust has delivered a net return of 12.7%.**
- **Based on our FY18 assumptions, the Trust represents considerable value with a price to free cash flow per share of 8.5 times, being a 42.0% discount to the ex-100 market.**

Market Review

Global markets were generally stronger in May, with the S&P500 up 1.2%, Nikkei 225 up 2.4% and FTSE100 up 4.4%, while the Shanghai Composite declined 1.2%. Commodity prices were softer, moving back to more sustainable levels as generally expected, with oil down 3.0%, iron ore down 17.0%, coking coal down 39.0% as cyclone supply disruptions reversed, thermal coal down 12.0% and copper down 1.0%, while gold was flat. The Reserve Bank of Australia left the cash rate steady at 1.5% and the Australian Dollar (AUD) finished the month down one cent at 74 US cents.

During May, the best performing sectors where information technology (up 5.0%), telecommunication services (up 4.6%) and industrials (up 3.0%). The worst performing sectors were healthcare (down 13.7%), utilities (down 6.4%) and consumer discretionary (down 4.5%).

Trust Review

The Trust ended up 0.4%, net of all fees, outperforming the Index (which closed down 2.1%) by 2.5%.

The strongest attributor to Trust performance was **EML Payments** (up 18.7%) following a detailed quarterly update that confirmed strong growth across all divisions and continued strong cash flow. The update also provided more detailed insights into the key drivers for each division and region, something which was poorly understood by the market previously.

Alliance Aviation (up 31.9%) announced a significant wet leasing deal with Virgin covering regional routes in Queensland. This will increase the fleet of Alliance by 11.0%, flying activity by 45.0% and begin to utilise the surplus aircraft previously purchased by Alliance from Austrian Air. Separately the ACCC also approved their strategic alliance with Virgin to jointly grow their fly-in-fly-out operations and share maintenance costs.

Melbourne IT (up 19.0%) announced an accretive acquisition of WME Group, which is expected to lift earnings per share by between 12.0% to 18.0%. WME significantly enhances the web design capability of Melbourne IT as well as providing digital marketing solutions.

Emerging Western Australian gold producer **Dacian Gold** (up 14.9%) commenced underground mining during the month and released positive drill results highlighting upside at their Mt Morgans mine.

The main detractor from performance was global hedge fund-of-fund manager **HFA** (down 10.0%) giving up all of the previous month's gains. There hasn't been any news flow since April's Funds Under Management update which reflected strong growth of 8.6% to US$9.5 billion post two new international mandate wins. HFA will benefit from a weaker AUD expected over the coming 12 months.

At the month-end closing price of $2.15, the stock is cheap on FY18 EV/EBIT of 5.1 times and a cash dividend yield of 10.7% and stands out when compared to funds management peers, the industrial sector and the market.

Quarter ended 31 March 2017				
USD	31 December 2016 AUMA	Net flows	Performance	31 March 2017 AUMA *(Estimate)*
		Note 1	Note 2 & 3	Note 3
Lighthouse Commingled Funds	USD 4.33 bn	↑ USD 0.02 bn	↑ USD 0.12 bn	**USD 4.47 bn**
Lighthouse Single Investor Customised Solutions	USD 4.40 bn	↑ USD 0.55 bn	↑ USD 0.06 bn	**USD 5.01 bn**
Total AUMA	USD 8.73 bn	↑ USD 0.57 bn	↑ USD 0.18 bn	**USD 9.48 bn**

Source: HFA Holdings March Update

Other weak performers included **Capral Aluminium** (down 23.5%) after providing a negative trading update citing continued tough conditions in the Western Australian housing market, stronger aluminium prices and the temporary drag on volumes from poor weather on the east coast.

Trust activity

Having sold two thirds of our position in **Automotive Holdings** during March and April, at an average price of $4.02 following two consecutive months of weaker new car sales data, we exited the remainder of the position during May, taking our average exit price to $3.47 (month end closing price $2.94). This was following a weak trading update that not only reflected the impact from weaker car sales, but a disappointing update on the progress of their troubled Logistics division that was supposedly meant to show significant improvement under new management during 2H17.

We also exited residential land developer **AV Jennings** given our view of the current housing cycle maturing and decided to take advantage of a liquidity event that presented for this relatively less liquid stock.

Proceeds were used to acquire a position in travel company **Helloworld** at an average price of $3.79 (month end closing price $4.01) which we view as an attractive valuation combined with our positive view on the tourism thematic.

At month end the Trust held 56 stocks and cash of 6.5%.

Outlook

The Trust offers considerable value trading on an FY18 price to earnings ratio of 10.7 times (29.0% discount to the ex-100 market) and a gross yield of 5.5% (14.0% premium to the ex-100 market).

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	3.6	5.8
Materials	15.2	16.3
Industrials	12.3	9.4
Consumer Discretionary	21.0	20.0
Consumer Staples	1.2	8.7
Health Care	6.8	6.6
Financials-x-Real Estate	11.6	8.6
Real Estate	5.9	15.3
Information Technology	7.6	6.4
Telecommunication Services	4.9	2.1
Utilities	3.4	0.7
Cash & Other	6.5	-

Rounding accounts for small +/- from 100%.

Signatory of:

PRI Principles for Responsible Investment