

| | Quarter | FYTD | 1 year | 3 years | 5 years | Since Inception [^] |
|--|------------|------------|------------|------------|------------|------------------------------|
| | % | % | % | % p.a. | % p.a. | % p.a. |
| Perennial Value Smaller Companies Trust* | 3.4 | 3.4 | 7.7 | 6.7 | 6.6 | 10.7 |
| S&P/ASX Small Ordinaries Accum. Index | 1.5 | 1.5 | -0.1 | 1.7 | -0.3 | 5.3 |
| Value Added (Detracted) | 1.9 | 1.9 | 7.8 | 5.0 | 6.9 | 5.4 |

*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 (as at 30 September 2014):

AUD117.2 million

Income distribution frequency:

Half yearly

Minimum initial investment:

\$25,000

Trust inception date:

March 2002

APIR code:

IOF0214AU

- ▶ **During the quarter the Trust outperformed the Index by 1.9%.**
- ▶ **The best performing stock in the Trust during the quarter was HFA Holdings (up 39.9%)**
- ▶ **The valuation of the Trust remains attractive relative to market.**

During the quarter, the Perennial Value Smaller Companies Trust (the Trust) returned 3.4% (net of fees) compared to the benchmark S&P/ASX Small Ordinaries Accumulation Index (the Index) return of 1.5%, resulting in outperformance of 1.9%.

Global markets were volatile during the quarter as a gradually improving US economy generated debate as to the likely impacts of the end of the US Federal Reserve's (the Fed) quantitative easing in the US and the timing of any interest rate increase. At the same time the market grappled with unrest in the Middle East and Ukraine, concerns over a slowdown in China and a still sluggish European economy. Despite this, the S&P500 (up 0.6%), Nikkei 225 (up 6.7%) and Shanghai Composite (up 15.4%) finished higher at end of the quarter while the FTSE (down 1.8%) finished lower.

Both globally and domestically, macro data was mixed. In the US, second quarter GDP growth came in at 4.6% on an annualised basis and employment data continued to show improvement while other data was more underwhelming, particularly towards quarter end. In China, the latest round of data indicates that growth is falling short of the official target, which prompted the announcement of additional bank liquidity measures to help stimulate growth. In Europe, the European Central Bank (ECB) also announced additional stimulus measures as growth remains barely positive. Domestically the unemployment rate remained at 6.1% despite some intra-period volatility after touching 6.4% in August. Consumer and business confidence remained stable over the quarter despite some more positive signs in August. Building approvals data was strong. The Reserve Bank of Australia (RBA) left the cash rate unchanged at 2.5%, however, hinted that it may be considering counter-cyclical credit controls to cool the strong housing market.

The AUD/USD weakened significantly over the quarter, ending the quarter at 87.2c down from 94.3c at the end of June. The Trust has many holdings which are well placed to benefit from a sustained weakening in the AUD/USD although in most cases this is yet to be reflected in stronger share prices.

The September quarter saw significant divergence in the performance of some sectors. The strongest performers were telecommunication services (up 14.3%), information technology (up 9.7%) and healthcare (up 8.2%). Detractors included materials (down 11.2%) and utilities (down 3.8%).

The best performing stock in the Trust during the quarter was HFA Holdings (up 39.9%) following the conversion of the last remaining convertible notes and the delivery of a FY14 result ahead of expectations. Post the clean-up of the convertible notes HFA has a clean and simple balance sheet and with the bulk of the earnings in USD they are well placed to benefit from the falling AUD/USD.

After delivering a solid FY14 result, the M2 Group (owners of iPrimus, Dodo etc.) (up 31.7%), showed an improvement in cashflow and subscriber growth ahead of market expectations.

Other strong performers included Boom Logistics (up 33.3%) and Sino Gas Energy (up 31.3%) as both stocks recovered from over-sold positions. Recent IPO's including

Mantra Group (up 30.0%) and Bellamy's Australia (total return of 34.2% over holding period) also contributed to performance.

Detracting from performance was BC Iron (down 44.8%) primarily due to the significant weakness in the iron ore price in the quarter. BC Iron remains the only iron ore stock in the Trust and has a relatively strong balance sheet and high margins compared to other small cap miners. Other detractors from the materials sector were Aquarius Platinum (down 19.0%) and Panoramic Resources (down 18.7%) again reflecting weakness in the respective underlying commodities.

Mint Wireless (down 34.9%) was also weaker as the market became concerned with competition from banks and technology companies in the mobile payment space. We remain of the view that the agreement Mint has with MYOB and Bank of New Zealand will begin to generate user growth from October when the product is officially launched. On our forecasts, the rollout with these clients alone justifies the current share price.

During the quarter, we exited our position in Abacus Property (at \$2.72 versus quarter end price of \$2.56) and BT Investment Management (at \$6.54 versus quarter end price of \$6.15) on valuation grounds. We also exited positions in recent floats Bellamy's Australia and Isentia Group after strong performances.

The proceeds were used to re-establish a position in Nufarm (at an average of \$4.27 versus quarter end price of \$4.93). The Trust also built a position in promising oil and gas producer Austex Oil (at an average price of \$0.20 versus quarter end price of \$0.225). The Trust has made several successful investments in the US shale oil space (such as Sundance Energy and Aurora Oil and Gas) and Austex Oil shares some of the same qualities which attracted us to these investments.

The valuation of the Trust remains attractive relative to market (as shown in the table below).

| Prospective FY15 | Price to Earnings (times) | Price to free cashflow (times) | Gross Yield (%) | Price to NTA (times) | Net Interest Cover (times) | 3yr EPS growth (%p.a.) |
|---|---------------------------|--------------------------------|-----------------|----------------------|----------------------------|------------------------|
| Market Average Ex-100* | 15.9 | 13.5 | 4.8 | 1.7 | 8.8 | 11.9 |
| Perennial Value Smaller Companies Trust** | 11.6 | 12.3 | 5.0 | 1.2 | 26.2 | 29.6 |
| Premium/ (Discount) to Market | (27%) | (9%) | 5% | (30%) | 198% | 149% |

Source: *Macquarie Securities, Goldman Sachs and UBS as at 29 September 2014. **Perennial as at 26 September 2014

Perennial Value Management remains alert to Environmental, Social and Corporate Governance (ES&G) issues in the Trust. During the quarter, Swick Mining demonstrated a 70% reduction in Total Recordable Injury Frequency Rate over two years. They also they have more research and development initiatives (such as automated rod handling) to rollout this year with the aim of achieving further improvements in both safety and productivity.

At month end, stock numbers were 58 and cash was 1.7%.

| Asset Allocation | | |
|----------------------------|----------------|----------------|
| Sector | Trust weight % | Index weight % |
| Energy | 11.9 | 7.4 |
| Materials | 14.1 | 15.0 |
| Industrials | 18.1 | 15.5 |
| Consumer Discretionary | 24.7 | 23.6 |
| Consumer Staples | 0.0 | 3.7 |
| Health Care | 2.3 | 6.2 |
| Financials-x-Real Estate | 7.4 | 6.8 |
| Real Estate | 12.7 | 10.1 |
| Information Technology | 3.9 | 4.3 |
| Telecommunication Services | 1.7 | 6.6 |
| Utilities | 1.5 | 0.6 |
| Other | 1.7 | - |

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:



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