Perennial Value Smaller Companies Trust

Monthly Report
31 January 2015

	Month	Quarter	FYTD	1 year	3 years	5 years	Since Inception^
	%	%	%	%	% p.a.	% p.a.	% p.a.
Perennial Value Smaller Companies Trust*	-1.3	-6.7	-8.7	-5.8	1.0	3.5	9.3
S&P/ASX Small Ordinaries Accum. Index	0.9	-2.5	-1.6	-0.2	-1.6	-0.3	4.9
Value Added (Detracted)	**-2.2**	**-4.2**	**-7.1**	**-5.6**	**2.6**	**3.8**	**4.4**

*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 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 January 2015):
AUD103.7 million

Income distribution frequency:
Half yearly

Minimum initial investment:
$25,000

Trust inception date:
March 2002

APIR code:
IOF0214AU

- **The Index gained 0.9% for the month, with the key driver being the gold sector.**
- **Tox Free Solutions (up 22.3%), the best performing stock in the Trust, announced a profit upgrade during the month.**
- **We exited our position in gold producer Regis Resources on valuation grounds following its strong rally and took profits in Super Retail Group and Whitehaven Coal ahead of its interim results.**

The S&P/ASX Small Ordinaries Accumulation Index (the Index) gained 0.9% during January. The Perennial Value Smaller Companies Trust (the Trust) declined 1.3% after all fees, underperforming the Index return by a net 2.2%.

Key drivers of the Index included a very strong performance from the gold sector following the announcement of quantitative easing from the European Central Bank, with most gold equities gaining 20% to 40%. The Trust, which benefited from a 50% gain in Regis Resources last month, is underweight the gold sector with inflation concerns low on the global economic agenda. Additionally, a range of Index-heavy stocks drove the benchmark. For example, fund managers Platinum Asset Management (up 20.2%) and Magellan Financial Group (up 15.9%) both trade on an IBES 12-month forward P/E of 22x, while Liquefied Natural Gas (up 23.1%) is not forecast to generate any earnings until 2018. The Trust does not own these stocks on valuation grounds and this impacted our relative performance in January 2015.

The European Central Bank’s announcement that it will be implementing quantitative easing at a level exceeding market expectations impacted global equity markets. Separately, the Swiss Central bank abandoned the Swiss Franc’s cap against the Euro. The oil price continued to fall, with the WTI oil price falling 9% over the month. Other commodities were also weak, with iron ore and copper both down 13%. Bond yields continued to fall sharply, with the US 10 year Treasury yield falling form 2.2% to 1.6% over the month. Global economic data was mixed. US retail sales were weak, China data remained soft and Eurozone deflation was worse than expected. However, more positively, US employment data was strong with the US unemployment rate falling to 5.6% and US consumer confidence jumped to the highest level since 2004.

Domestic economic data was generally positive, employment was stronger than expected in December with the jobless rate unexpectedly falling and housing credit up 7.1% over the year to December, the strongest growth since December 2010. The Australian cash rate remained unchanged at 2.5% during January and the Australian dollar reached a 5-five year low against the US dollar, falling from 81 to 78 US cents.

The strongest performing sectors were materials (up 6.2%) largely driven by the gold stocks, financials ex property trusts (up 5.9%) and property trusts (up 3.1%). The weakest sector was industrials (down 7.1%) and information technology (down 2.2%).

The best attributor during the month was hazardous waste management service provider Tox Free Solutions (up 22.3%). Despite deriving over a third of its revenue from the energy and mining sectors, the company announced a profit upgrade during the month. We increased our exposure late last November (at average $2.25 versus January month end 291c) subsequent to the fall in the oil price, having just returned from visiting their resource recovery assets in Karratha, WA.

Perennial Value on site at Tox Free Solutions' centre in Karratha, WA- November 2014

Medical equipment distributor Life Healthcare Group (up 22.2%) announced a profit upgrade following 15% growth in revenue as the company continues to take market share in the implantable device market (mainly spine) and expand its cardiac business.

Super Retail Group (up 22.1%) benefited from broker upgrades, with lower petrol prices expected to benefit discretionary spend, especially at their Super Cheap Auto chain of stores. Ferry owner and operator Sealink (up 15.0%) is also a beneficiary from lower fuel prices, coupled with healthy inbound tourism courtesy of a weak Australian dollar.

The main detractor in January was marine logistics and supply-base service provider MMA Offshore (down 35.5%). The company continues to be out of favour with investors amidst a weaker oil price. With a healthy balance sheet (net debt/EBITDA of 1.0x) and an asset base which includes over 88 vessels and irreplaceable supply bases in Dampier and Broome, WA, we feel there is value with the share price trading at 0.39x net tangible assets, making it the cheapest amongst global listed peers (greater than $300 million market cap).

Sino Gas Energy (down 28.9%) released its December quarterly activities statement which by all accounts was a good report. We are of the view that the stock was sold off on concerns that a weaker oil price will drag the gas price lower. It is worth noting that China gas prices are set by the NDRC and are not linked to oil prices. Further, the 2020 Energy Development Strategy Plan aims to increase natural gas share of energy mix from 4.4% (2011) to +10% by 2020, with price being a key means of incentivising new supply.

Other detractors included Matrix Composites & Engineering (down 19.2%) on concerns a weaker oil price will impact future deep offshore oil projects. We will continue to monitor our position in this company, which announced US64 million of new contracts in the December quarter, thereby providing revenue visibility for CY15.

Hillgrove Resources (down 15.6%) was sold off on a weaker copper price despite the company updating the market during the month on its hedging program which now sees 78% of its production through to March 2016 covered at average AUD3.50 per pound copper (versus month end closing price AUD3.21).

In terms of portfolio activity, we exited our position in Ausenco given our concerns over its balance sheet as no significant new contracts have been awarded for some time amidst weaker commodity prices. We also exited our position in gold producer Regis Resources on valuation grounds following its strong rally. Profits were taken in Super Retail Group and Whitehaven Coal ahead of its interim results. Proceeds were used to establish a position in low-cost copper producer Sandfire Resources given the fall in the price of copper to date coupled with the Chinese government announcing capex plans for the Chinese power grid which will require equivalent to 11% of global copper demand alone.

At month end, stock numbers were 52 and cash was 3.4%.

Asset Allocation

Sector	Trust weight %	Index weight %
Energy	7.8	5.0
Materials	9.6	15.0
Industrials	18.1	13.9
Consumer Discretionary	28.5	24.6
Consumer Staples	0.0	4.2
Health Care	1.8	6.5
Financials-x-Real Estate	10.5	8.3
Real Estate	13.9	11.8
Information Technology	3.0	4.7
Telecommunication Services	2.0	5.3
Utilities	1.3	0.7
Other	3.4	-

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