Perennial Value Smaller Companies Trust

Monthly Report as at 31 December 2013

	1 Month %	3 Months %	FYTD %	1 Year %	3 Years % p.a.	5 Years % p.a.	Since Inception^ % p.a.
Perennial Value Smaller Companies Trust+	0.8	0.2	19.1	-3.7	-0.3	14.7	10.7
S&P/ASX Small Ordinaries Accum. Index	2.6	-0.1	14.7	-0.8	-6.0	8.1	5.6
Value Added (Detracted)	**-1.8**	**0.3**	**4.4**	**-2.9**	**5.7**	**6.6**	**5.1**

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

- Despite a slow start and early losses, the small companies sector finished the month up 2.5% December.
- For the financial year to date, the Trust has delivered a net return of 19.1% and outperformed the Index return by 4.4%.
- TPG Telecom (up 28.8%) was a key performer for the Trust for the month.

The smaller end of the Australian equity market sagged at the start of December under the weight of negative company earnings updates coupled with significant new equity issuances from a spate of IPOs flooding the market. Additionally, investors had to contend with the decision by the US Federal Reserve to begin tapering its bond buying program, thereby reducing purchases by USD10 billion to USD75 billion per month from January 2014.

Despite the poor start, local equity markets took this news flow in its stride with the benchmark the S&P/Small Ordinaries Accumulation Index (the Index) down reversing early losses to end the month up 2.6%. After initially outperforming at the start of the month, the Perennial Value Smaller Companies Trust (the Trust) ended the month up 0.8% net of all fees, thereby underperforming the Index return by 1.8%. While this is a disappointing outcome, readers will note that the Trust had enjoyed consecutive monthly net outperformance in each of the five months prior to December.

For the financial year to date, the Trust has returned 19.1% net of all fees against the Index return of 14.7%, thereby outperforming by a net 4.4%.

The best performing sectors in the Index were telecommunications (up 5.9%) where the Trust has an underweight position, utilities (up 0.6%) and energy (up 0.1%). Materials, where the Trust is currently underweight, followed November to again be the worst performing sector (down 7.3%), followed by industrials (down 4.7%) and information technology (down 4.6%).

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	**Risk Profile:** High
Trust FUM (as at 31/12/13): AUD135.6 million	**Income Distribution Frequency:** Half yearly
Trust Inception date: March 2002	**Minimum Initial Investment:** $25,000
	APIR code: IOF0214AU

*Excluding performance fees.

Domestic data was mixed, with Q3 GDP growing below trend at 2.3% p.a., unemployment rising marginally to 5.8% and business confidence slipping, while building approvals and retail sales improved. The Reserve Bank of Australia (RBA) left interest rates on hold at 2.5% and the Australian dollar continued its decline, finishing the month down 2 cents at USD0.89.

A key performer for the Trust during December was TPG Telecom (up 28.8%) following a positive AGM update and its astute purchase of AAPT from Telecom New Zealand. This earnings accretive acquisition provides TPG with fibre infrastructure and should assist the company in expanding into the lucrative SME market. While we view this deal very favourably, we took some profits during the month following stellar share price gains, in line with our investment process given the company's valuation metrics.

Matrix Engineering (up 19.5%) did not release any information to the market, however, our company meetings in both WA and the USA during November confirmed improving conditions for its end market. This coupled with a weakening Australian dollar (given a large majority of its earnings are derived from sales offshore), suggests a solid outlook for Matrix.

iSelect, a stock we avoided when the company floated in June at $1.85, whereafter we built a position from September to December at an average price of $1.33 (approximately 28% below issue price), rallied strongly (up 18.4%) to finish the month at $1.44. The company did not release any material news flow during the month, but we did catch up with the founder and chairman to get an update on its strategy following recent management changes. iSelect should be a beneficiary from the private health insurance premium rises as policyholders look to get a better deal in light of the Federal Minister for Health signing off on 2014 premium increases of 7% to 8%.

Whitehaven Coal (up 17.9%) announced that its Maules Creek approval had been upheld in Federal Court, which together with its recent debt realignment and gradually improving global coal prices, bodes well for this coal company's future.

Other strong performers included PanAust (up 18.8%), PMI Gold (up 16.7%) after the company received a takeover offer from Canadian listed Asanko, BT Investments (up 16.5%) and Webjet (up 15.3%).

Crowe Horwath (down 42.0%) announced a significant earnings downgrade due to weak demand for discretionary business advisory services in both Australia and New Zealand. We continue to monitor this position closely, mindful it was only in February 2013 that this company received a takeover offer. Ausenco (down 40.9%) resumed trade after its earnings downgrade and capital raising in late November. Energy Action (down 22.4%) announced a downgrade, with revenue growth expected to now be 15% versus 28% previously, as the benefits of its sales force and related incentive restructure program, which commenced earlier this calendar year, takes longer than anticipated to gain traction. We used the share price weakness to add to our position, given we had taken some profits prior to this downgrade.

The Trust's performance was also impacted by a plethora of mining services companies not held in the Trust clawing back some underperformance, such as Forge Group (up 132.0%), Decmil (up 33.3%), Ausdrill (up 32.1%), Boart Longyear (up 28.3%), Sedgman (up 23.6%), RCR Tomlinson (up 22.8%), Macmahon Holdings (up 20.8%). In general terms, we are of the view that at this juncture it is too soon to invest in mining service companies concentrated at the exploration end. Boart Longyear is one such company, which in addition to its weak balance sheet, fails to get through our investment process. And it was only a month ago that Forge revealed two material problem contracts likely to result in the breaching of its banking covenants.

A combination of the aforementioned, coupled with our underweight position in the strongly performing telecommunications sector resulted in the Trust's underperformance this month.

After taking decent profits in November at an average price of $4.95, we added to our position in NuFarm following a share price retracement in December at an average price of $4.27 (month end closing price $4.39). We have spent the past two months sifting through a barrage of companies seeking a public listing. Data analytics and credit information provider Veda Group was one of the companies we decided to invest in given its dominant market share coupled with private equity retaining a material stake post IPO. Mindful of its December IPO valuation metrics at the $1.25 issue price, we took profits and exited this position at an average price of $1.66 on valuation grounds. Proceeds were used to re-establish a position in Mermaid Marine following a material sell off in its share price after announcing that interim earnings will be impacted due to the delay in commencement of a few contracts. Having also visited management in mid-November in Freemantle, WA, we retain the view that Mermaid is a well-run company, with earnings growth to be underpinned by construction and production activity in the Australian offshore oil & gas sector.

At month end, stock numbers stood at 57 with cash at 2.3%.

Asset Allocation as at 31 December 2013

Asset Class	Trust Weight %	Index Weight %
Energy	12.8	7.2
Materials	11.3	17.5
Industrials	14.7	16.7
Consumer Discretionary	27.6	26.6
Consumer Staples	1.4	2.4
Health Care	2.6	4.4
Financials-x-Real Estate	4.9	6.3
Real Estate	13.7	9.5
Information Technology	3.9	2.3
Telecommunication Services	2.6	5.5
Utilities	1.6	1.6
Other	2.8	0.0

Rounding accounts for small +/- from 100%.