Perennial Value Microcap Opportunities Trust

MONTHLY REPORT FEBRUARY 2020

	Month (%)	Quarter (%)	FYTD (%)	1 Year (%)	3 Years (% p.a.)	Since Inception^ (%p.a.)	Since Inception Cumulative^ (%)
Perennial Value Microcap Opportunities Trust (Net)	-11.3	-9.0	0.9	13.7	20.8	20.8	78.8
S&P/ASX Small Ordinaries Accumulation Index	-8.7	-5.9	-1.9	1.6	8.3	8.6	28.7
Value Added	**-2.6**	**-3.1**	**2.8**	**12.1**	**12.5**	**12.2**	**50.1**

^Since inception: February 2017. Past performance is not a reliable indicator of future performance.

Overview

February finished with the largest sell-off in financial markets since the GFC given concerns about the demand impact from the spread of the Coronavirus. Investors were desperate for liquidity and sold irrespective of whether companies were directly impacted. For example, the gold sector sold off (ASX gold index down 4.1%) despite the A$ gold price being up 5.3% for the month. Investors ignored the improving outlook for gold equities, instead selling them for liquidity. We use gold equities to partially hedge our more cyclically exposed industrial portfolio and thus, without this offset working, our portfolio was down 11.3% (net of all fees) compared to the Small Ordinaries Index which was down 8.7%.

Looking forward, such a large indiscriminate sell-off creates great investing opportunities. We await signs of a bottoming in demand before adding to resources and also think it is too early for travel stocks and other directly affected sectors. However, there are many stocks in the portfolio that displayed positive fundamentals in the February reporting season and were ignored given 'macro' concerns. Over time, these stock-specific attributes will shine through. In the meantime, the portfolio is the best value it has been since the GFC at 9.3x FY21 earnings (a 45.0% discount to the Index). The portfolio also holds three industrial stocks now trading below hard book value.

Perennial Value Microcap Opportunities Trust

The aim of the Trust is to grow the value of your investment over the long term by investing in a portfolio of Australian companies that are either listed or unlisted companies found outside the S&P/ASX Top 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

Andrew Smith and Sam Berridge

Trust FUM

AUD $179 million

Distribution Frequency

Annual

Minimum Initial Investment

$25,000

Trust Inception Date

February 2017

Fees

1.20% p.a. + Performance fee

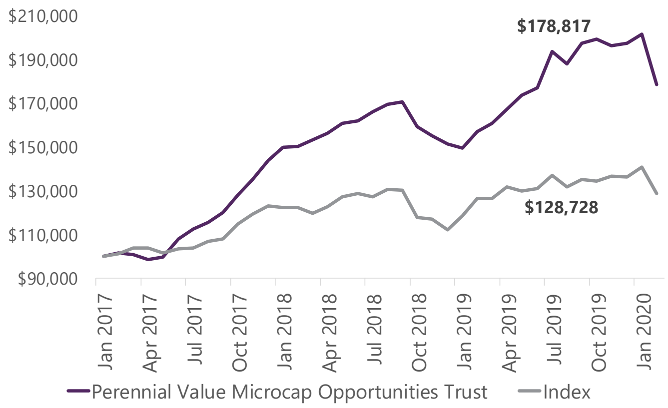
APIR Code

WPC3982AU

Top 5 Positions

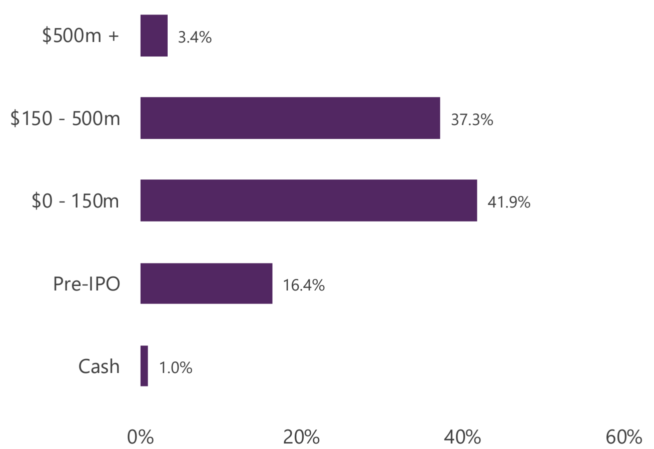
Top 5 Positions	Trust (%)	Index (%)
SWICK MINING SERVICES LTD	4.6	0.0
ALLIANCE AVIATION SERVICES L	3.1	0.0
LIMEADE INC	3.0	0.0
JANISON EDUCATION GROUP L	2.6	0.0
LONGTABLE GROUP LTD	2.6	0.0

Growth of $100,000 Since Inception

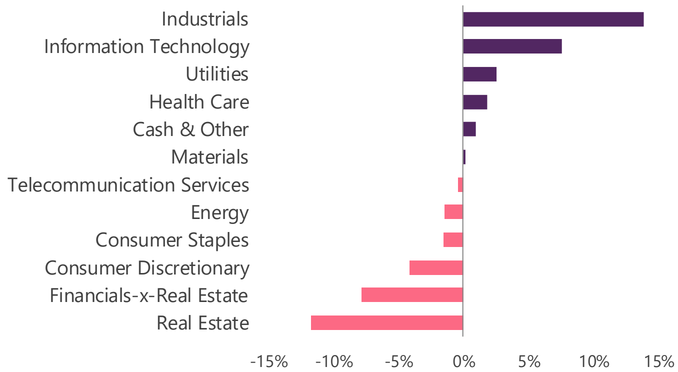


Performance shown net of fees with distributions reinvested. Does not take into account any taxes payable by an investor. Past performance is not a reliable indication of future performance.

Market Capitalisation Exposure



Sector Active Exposure vs Index



Trust Review

February finished with the largest sell-off in financial markets since the GFC given concerns about the demand impact from the spread of the Coronavirus. Investors were desperate for liquidity and sold irrespective of whether companies were directly impacted. For example, the gold sector sold-off despite the A$ gold price being up 5.3% for the month. Investors ignored the improving fundamentals for gold stocks and instead sold them for liquidity (see attached chart).

For investors looking forward, this detachment from fundamentals creates great investment opportunities. For now, we are focusing on companies with the least exposure to the slowdown caused by Coronavirus and which have also been caught in the widespread selloff.

In this vein, there were many positive results reported late in the month that were ignored given a very distracted market:

- **PWR Holdings** (down 9.1%) posted revenue growth of 20% on increasing margins, resulting in EBITDA growth of 34% year-on-year and a net cash balance of $7.9m.
- **Limeade** (down 1.6%) reported 20% growth in annual contract value, with closing net cash of US$32m.
- **MoneyMe** (+7.3%) reported 112% growth in the loan book and is now well positioned to significantly exceed prospectus forecasts.

HRL Holdings (+12.0%) reported early in the month and did benefit from investor interest in the turnaround story that is unfolding. Revenues increased by 15.6% and more importantly, margins recovered strongly with EBITDA margins recovering to 16.0% from 5.0% in the prior period.

One stock that may benefit from the Coronavirus is **Genetic Signatures** (down 3.9%). The company disclosed that their 3base™ test can detect the latest strain of the Coronavirus and they are focusing significant resources on further market development of their test as a result.

Source: Perennial Value and Bloomberg

Austin Engineering (down 26.2%) reported a mixed 1H20 with order delays into the 2H but high cash generation which significantly improved the balance sheet. The market seemed concerned with the large skew of earnings to the 2H but management reconfirmed guidance given revenue forecasts are 90% covered by existing orders.

The main stock with a direct impact from the Coronavirus was **Atomos** (down 40.8%). The 1H20 result was solid with both revenue and EBITDA growth of 35% driven by new products clearly gaining traction. However, the market focused on the potential supply chain disruptions which could impact product flow going forward. We now expect some delays to the new Neon product but thanks to a large pre-Christmas restock, core product inventory is sufficient to meet forecast demand in April, and the latest update suggests the key factories are at least partially back on line. The improving traction Atomos is having with customers and growing brand presence will be the long term driver of value rather than the short term supply issues – hence we were buying on weakness.

Primero Group (down 42.9%) presented 1H20 accounts which showed PGX hadn't been paid for its largest contract during the period, with $45m outstanding at the end of December. Investors reacted savagely with the current share price now implying no recovery of these costs and further balance sheet pressure. We are more comfortable and view further downside as limited. By contrast, there are several sources of upside (not least being the recovery of monies owning by Wartsila), hence we believe the risk/reward is compelling at these levels.

At month end we held 70 positions and cash of 1.0%.

Market Review – Australia (%)

S&P/ASX Small Ordinaries Index	-8.7
Energy	-21.8
Materials	-10.6
Industrials	-11.0
Consumer Discretionary	-5.7
Consumer Staples	-7.9
Health Care	-14.1
Financials-x-Real Estate	-10.5
Real Estate	-1.6
Information Technology	-15.5
Telecommunication Services	-10.4
Utilities	-6.6

Microcap Portfolio Managers: Sam Berridge (left) and Andrew Smith (right)

Contact Us

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