PERENNIAL VALUE MANAGEMENT

Perennial Value Smaller Companies Trust

Monthly Report
30 November 2016

	Month	Quarter	FYTD	1 year	3 years	5 years	Since Inception^
	%	%	%	%	% p.a.	% p.a.	% p.a.
Perennial Value Smaller Companies Trust*	-1.9	-0.4	11.0	12.8	6.7	6.3	9.9
S&P/ASX Small Ordinaries Accum. Index	-1.2	-4.4	2.1	13.5	5.9	3.2	5.5
Value Added (Detracted)	**-0.7**	**4.0**	**8.9**	**-0.7**	**0.8**	**3.1**	**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 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 November 2016):
AUD $111 million

Income distribution frequency:
Half yearly

Minimum initial investment:
$25,000

Trust inception date:
March 2002

APIR code:
IOF0214AU

- **November was a volatile month dominated by the US election and Australian companies hosting their annual general meetings.**
- **The Perennial Value Smaller Companies Trust (the Trust) underperformed the S&P/ASX Small Ordinaries Index (the Index) by 65 basis points net of all fees.**
- **The Trust offers good value trading on a 12.8 times FY17 price to earnings ratio (P/E) and a 9.9 times FY18 P/E ratio, representing a discount of 23.0% and 33.0% respectively to that of the Index.**

Trust Performance

The Index fell 1.2% during the month. The Trust ended down 1.9%, net of all fees, underperforming by a net 0.7%.

Financial year to date, the Trust is up a net 11.0%, outperforming the Index by 8.9% net of all fees benefiting from the market moving away from high P/E expensive and momentum stocks towards those that offer value.

The key development over the month was the result of the US election. International markets generally reacted positively, with the S&P500 up 3.4%, Nikkei 225 up 5.1% and Shanghai Composite up 4.8%, while the FTSE 100 declined 2.5%. The month saw strong rallies in iron ore (up 24.6%) and hard coking coal (up 20.2%), while oil rose also 6.7%. Thermal coal declined 23.7% from its recent high and gold declined 7.7%. The Federal Reserve left rates unchanged, as did the Reserve Bank of Australia, with the cash rate remaining steady at 1.5%, while the Australian Dollar finished the month down 2 cents at 0.74 US cents.

Sector performance for the Index was negative across the market, with only consumer staples (up 5.2%) and financials ex-property trusts (up 2.0%) finishing in positive territory. The worst performing sector was healthcare (down 5.4%) followed by information technology (down 4.1%).

The worst performing stock was Adairs (down 35.5%) which lowered their earnings guidance due to a fashion misread in their bedlinen range, resulting in the company marking down product to clear their inventory. Whilst a disappointing outcome, it is not uncommon amongst specialty retailers to misinterpret the fashion trends, indeed accessories specialty retailer Lovisa experienced a similar issue over the 2015 racing carnival season, leading them to downgrade earnings significantly, which provided a very good buying opportunity as their share price recovered strongly a year later. We used the weakness in Adairs to add to our relatively small position by acquiring stock at an average price of $1.50 (month-end closing price $1.65). It was also pleasing to see various directors buying decent amounts of shares on market too.

Diagnostic Imaging service provider Integral Diagnostics (down 27.8%) downgraded earnings at their annual general meeting due to cost growth running ahead of revenue growth, given the volatile nature of demand at present.

The so called "Trump reflation' trade triggered a rotation into cyclical stocks that benefitted commodity prices too. One of the best contributors during the month was low-cost nickel producer Western Areas (up 28.3%), which benefitted from nickel's 7.0% rise and improved terms for its offtake. Low nickel prices earlier in the year, poor weather and Philippine Government production bans have all contributed to low stocks of nickel ore at Chinese ports. As we move into the Philippine wet season (Oct – Feb), that ore shortage is providing a positive driver for nickel prices. IGO (up 6.6%) was also a beneficiary of the positive move in the nickel price over the month. IGO produced first concentrate from its newly commissioned Nova nickel mine on budget and a month ahead of schedule (which is a rare occurrence in the small resources space!). When fully ramped up, Nova will be the lowest cost nickel mine in Australia.

Oz Minerals (up 21.0%) benefitted from copper's very strong gains, with the metal rising almost 20.0%.

Source: Perennial Value Management, Small cap resources and energy analyst Sam Berridge on site at Oz Minerals' Prominent Hill mine

Life Healthcare (up 11.0%) benefitted from their products being excluded from the prosthesis list cuts announced by the Government, coupled with the Company reconfirming guidance at their annual general meeting.

The Trust participated in the Initial Public Offer of recreational vehicle renter Apollo (up 35.0%) that successfully floated during the month.

Other stocks that performed well were GUD (up 8.9%), AVJennings (up 8.8%) and Austin Engineering (up 7.7%) with the company raising capital to provide working capital owing to a significant pick up in order activity with 2H17 earnings ahead of FY16.

Trust activity

The position in Fantastic Holdings was exited on market as the share price moved close to the takeover bid announced in October.

Proceeds were used to establish a position in Myer at an average price of $1.13 (month end closing price $1.28) following their better than expected 1Q17 sales update. Following their share price derating, we also established a position in Super Retail at an average price of $9.13 and took a few short-term profits later in the month at an average of $9.72 (month-end closing price $9.61).

We profitably exited our position in mining services provided NRW Holdings and used the proceeds to participate in the Austin Engineering capital raising at 16 cents per share for the reasons mentioned above. We subsequently took some profits at an average price of 22 cents per share in order to manage our exposure.

The Trust ended the month with 58 stocks and cash of 1.0%.

Outlook

Despite the derating in some expensive stocks during the month, there are still many small cap stocks trading on lofty price-to-earnings multiples (which we do not hold in the Trust as they do not meet our value process) and little margin of safety. The Trust offers value trading on 12.8 times FY17 P/E and 11.8 times price/free cash flow, representing a very significant 23.0% and 28.0% discount respectively to the ex-100 market.

As always, our focus will continue to be on investing in quality companies which are offering attractive valuations.

wsAsset Allocation

Sector	Trust weight %	Index weight %
Energy	5.1	4.7
Materials	13.6	20.1
Industrials	10.2	10.9
Consumer Discretionary	28.9	20.9
Consumer Staples	2.1	6.8
Health Care	6.7	6.4
Financials-x-Real Estate	6.9	8.6
Real Estate	13.0	11.4
Information Technology	7.7	8.0
Telecommunication Services	2.6	1.5
Utilities	2.3	0.8
Cash & Other	1.0	-

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