PERENNIAL VALUE MANAGEMENT

Perennial Value Smaller Companies Trust

Monthly Report
31 January 2017

	Month	Quarter	FYTD	1 year	3 years	5 years	Since Inception^
	%	%	%	%	% p.a.	% p.a.	% p.a.
Perennial Value Smaller Companies Trust*	-1.1	1.6	14.8	23.3	7.4	6.2	10.0
S&P/ASX Small Ordinaries Accum. Index	-2.4	-0.1	3.2	16.4	6.4	2.8	5.5
Value Added (Detracted)	**1.3**	**1.7**	**11.6**	**6.9**	**1.0**	**3.4**	**4.5**

*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 31 January 2017):
AUD $111 million

Income distribution frequency:
Half yearly

Minimum initial investment:
$25,000

Trust inception date:
March 2002

APIR code:
IOF0214AU

- **The market declined in January, with the S&P/ASX Small Ordinaries Accumulation Index down (the Index) 2.4%.**
- **The Trust declined 1.1% net of all fees, thereby outperforming the Index by 1.3%.**
- **The Trust offers good value trading on a 13.0 times FY17 P/E (Price to Earnings Ratio) and 10.4 times FY18 P/E, representing a discount of 22.0% and 29.0% respectively to that of the Index.**

Trust Performance

The Index fell 2.4% during the month. The Perennial Value Smaller Companies Trust (the Trust) ended down 1.1%, net of all fees, outperforming by a net 1.3%.

Global markets were mixed following their strong recent advances, with the S&P500 and Shanghai Composite both up 1.8%, while the FTSE100 (down 0.6%) and Nikkei 225 (down 0.4%) declined. Commodity prices diverged, with stronger metal prices seeing iron ore (up 3.0%), copper (up 8.0%) and gold (up 5.0%) all rising, while oil (down 2.0%), thermal coal (down 13.0%) and coking coal (down 26.0%) declined. The Reserve Bank of Australia (RBA) left the cash rate steady at 1.5%, while the Australian Dollar (AUD) finished the month strongly, up four cents at 0.76 US cents.

During January, the better performing sectors where telecommunication services (up 3.0%), energy (up 2.5%) and materials (up 1.7%). The worst performing sectors were information technology (down 9.9%) largely driven by a steep earnings downgrade from Aconex, which was not held by the Trust given its demanding valuation. Healthcare (down 5.9%) was dragged lower by a significant earnings downgrade from Virtus Health, which saw peer Monash IVF Group trade similarly lower (neither of these stocks are held in the Trust given our concerns over regulatory risk).

The best performing stock was Mint Payments (up 47.5%). The company hosted an investor day which highlighted their growth prospects in Asia as well as the quality of their relationship with large and strategic operators such as NETS (Singapore), BNZ (New Zealand) and Global Payments (listed on NYSE).

Eastern Goldfields (up 34.5%) rallied strongly on a recovery in the gold price, improved gold sentiment, a steady stream of positive exploration results and improved confidence that the debt facilities put in place in December will offset the need for further equity (at least in the short term). While still at an early stage (first gold production expected in March), following multiple site visits we have developed an appreciation for the exploration potential and gold endowment of their land holding. While we generally ascribe zero value to exploration potential, in Eastern Goldfield's case existing gold intersections across numerous resources outside of the current mining plan lead us to believe further increases in resources and reserves are highly likely.

Perennial Value's small cap resources analyst (Sam Berridge) on an Eastern Goldfields site visit to Davyhurst mine, WA, January 2017

Pacific Energy (up 19.3%) announced contract wins totalling 18 megawatts of additional power generation capacity, an increase of 7.5% on the exit rate at June 30. The wins came from a mix of new customers and organic growth from existing clients. Despite its utility like earnings stream, the stock continues to trade at a discount to the market. With its defensive earnings and positive growth outlook, we expect this discount to close over time.

Swick Mining (up 18.9%) continued to benefit from positive sentiment surrounding exploration spend. In our meetings with mining companies throughout January, a consistent theme was increased turnaround time for assay results from the labs in Perth and Kalgoorlie. Implying that drilling activity was strong up to and through the Christmas period. Further, the major miners appear to be joining the mid-cap miners in increasing exploration spend. A sign that this thematic still has some way to go.

Imdex (up 18.3%) responded to an increase in broker estimates based off better commodity prices and lifting exploration activity. We expect this to lead to increased activity for Imdex.

New Zealand media and entertainment business NZME (up 18.2%) recovered from an oversold position, benefitting from the proposed merger update with Fairfax New Zealand saying that it continues to progress with the New Zealand Commerce Commission process.

Stocks which detracted from performance included Sino Gas & Energy (down 13.0%) which gave production guidance towards the end of the month that was below expectations. Having increased production materially in the December quarter, the market was expecting more of the same in CY17. Instead Sino guided to flat production, preserving cash while it progresses the necessary approvals for full field development. This in turn should open up debt funding options towards the end of CY17.

Australian Agricultural Company (down 13.6%) was softer following the departure of their CFO during the month. We continued to reduce our position following their 1H17 result that was released in late November and reflected poor operating cash flow.

Trust activity

During the month, we took profits and exited Abacus Property at an average price of $2.99 given its premium to NTA (month end price $2.81). Also during the month, the Indonesian Government announced that it will be lifting bans on nickel exports. Prior to this announcement, we had been taking profits in each of Western Areas and Independence Group as both had rallied significantly and were trading at premium valuations. Following this Indonesian update, we exited Western Areas completely at an average price of $2.96 (month end price $2.45) and materially reduced our Independence Group position at an average price of $4.06 (month end price $3.77).

Proceeds were used to build positions in Doray Minerals (to add to our gold exposure) and Mantra Group following a material share price retracement that led to value emerging.

Outlook

Despite the continued derating in some expensive stocks during the month, there are still many small cap stocks trading on lofty price-to-earnings multiples providing little margin of safety (we do not hold these in the Trust as they do not meet our value process). The Trust offers value trading on 13.0 timesFY17 P/E and 12.3 times price/free cash flow, representing a healthy 22.0% and 20.0% 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.

Asset Allocation		
Sector	**Trust weight %**	**Index weight %**
Energy	4.2	5.0
Materials	14.8	21.0
Industrials	10.9	10.1
Consumer Discretionary	27.0	21.5
Consumer Staples	0.8	6.2
Health Care	5.4	6.2
Financials-x-Real Estate	9.1	8.7
Real Estate	10.3	13.1
Information Technology	7.4	5.8
Telecommunication Services	4.2	1.5
Utilities	2.7	0.9
Cash & Other	3.2	-

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