

CELESTE

Funds Management

Celeste Australian Small Companies Fund

Monthly update 31 January 2014

Fund Performance

The Fund was down 3.8% in January, with its benchmark, the ASX Small Ordinaries Accumulation Index down 2.8%. In January the ASX All Ordinaries Accumulation Index was also down 2.8%. Most global indices were lower. The S&P 500 was down 3.6% and NASDAQ down 1.7%. The FTSE was down 3.5%, the DAX down 2.6%, with the Nikkei down 8.5%. Other Asian markets fell with Korea's KOSPI down 3.5%, Hong Kong's Hang Seng down 5.5% and the Shanghai Composite down 3.9%. In the past year the Fund is down 4.4%, net of all fees, compared to a 7.4% decline in the S&P/ASX Small Ords Accumulation Index. Since inception in May 1998 the Fund's return is 15.6% pa, against the Index's 5.0% pa.

Portfolio Commentary

Sunland Group was up 14.6%. It announced the acquisition of a 4.0ha site in North Kellyville for \$7.2m. The site is expected to yield around 60 house and land products with end-value of \$42m. This represents further incremental geographic diversification and takes the total land bank in NSW to in excess of 500 products valued at \$310m. This represents around 10% of Sunland's portfolio.

Western Areas rose 12.7% on the back of a solid December quarter production report. Cash costs were well contained, the bank balance grew and the company remains soundly placed to exceed its full year production guidance. The Flying Fox and Spotted Quoll underground nickel mines have consistently delivered high grade ore, quarter after quarter. The investment proposition is supported by the company's ample mine life, relatively low cash costs and the opportunity to expand its Forrestania production at low incremental capital cost in the event of a more robust nickel price.

Skilled Group declined 16.2%. The market rotation away from stocks with 'perceived earnings risk' played heavily on companies exposed to mining & manufacturing. Thomas & Coffey shareholders approved the sale of their maintenance and asset management businesses to Skilled for \$33.5m, with \$7m in underlying EBITDA pre synergies anticipated. Post integration with the ATIVO business, the acquisition EV/EBITDA multiple will be <3x. The move is consistent with Skilled looking to grow its exposure to higher margin businesses with contracted revenues and recurrent cashflows.

Nufarm declined 11.6%. The company announced a market update indicating that its first half EBIT would fall towards the lower end of its guidance range. This outcome reflected unfavourable seasonal conditions in Australia with hot and dry weather prevailing over the summer. Contrastingly, South America delivered a stronger result with Brazil in particular, performing well. The majority of Nufarm's earnings are delivered in the second half period, and as such, reasonable climatic conditions should deliver a stronger full result than was the case in 2013.

Portfolio Top 5 Holdings

| Stock | % of Fund |
|---------------------------|-----------|
| 1 TRANSPACIFIC INDUSTRIES | 5.2 |
| 2 BREVILLE GROUP | 4.0 |
| 3 SKILLED GROUP | 3.8 |
| 4 MACA | 3.7 |
| 5 BC IRON | 3.7 |

Monthly Commentary

Equity investors around the world moved into 2014 hesitantly, dialling down their risk appetites and stock exposures accordingly. Apprehension seemed to focus on global growth expectations, with a focus on China, and on stimulus initiatives in the US.

In January investors needed to deal with the US Federal Open Market Committee (US Fed.) cutting their monthly bond purchases by US\$10b to US\$65b as economic activity continued to improve. As the US Fed noted, "...in light of cumulative progress towards maximum employment and the improvement in the outlook for labour market conditions, the committee decided to make further measured reductions in the pace of its asset purchases." To assuage investor concern on the pace of likely interest rate increases the US Fed did note that, "...a highly accommodative stance of monetary policy will remain appropriate for a considerable time..." and that "...the committee also reaffirmed its expectation that the current exceptionally low target range for the federal funds rate of 0 to ¼% will be appropriate for as long as unemployment remains above 6 ½%". Interestingly the Jan. FOMC meeting was the first one since 2011 where all 10 members of the US Fed voted in favour of a reduction in the asset purchase program.

Australian economic data in January was patchy with unemployment at 5.8%, as the participation rate fell, and Dec. quarter CPI rose a surprising 2.7%, bearing the brunt of the H2 2013 decline in the \$AUD. In the US Q4 GDP was 3.2% with consumption growing by a healthy 3.3%, and aggregate business investment up 3.8%. The US unemployment rate finished 2013 at 6.7%, compared to 7.9% one year ago. Eurozone unemployment in December was 12%, stable since October, with youth unemployment at 23.8%, largely unchanged over the year.

In China the Year of the Horse was welcomed by broadly supportive data with 2013 economic growth of 7.7% and inflation at a manageable 2.6%. Industrial output was up 9.7% in 2013, slightly less than the 10% achieved in 2012. Retail sales in China grew strongly in 2013, up 13.1%, whilst urban consumption rose 12.9% and rural consumption grew 14.6%, year on year. In January the China Railway Corporation noted that China's railway network had now topped 100,000km in total mileage, which compares with 225,000km in the US.

We expect that the forthcoming interim reporting season will lead to modest revisions in earnings expectations, and that levels of volatility will be elevated in the short term. We expect that the dramatic decline of the \$AUD in 2013 will create some operational headwinds for the corporate sector in the medium term, and that this will be a feature of reporting season commentary. We look towards interim reporting season opportunistically and will add to the portfolio, in a process consistent manner, when fundamentals are attractive and valuations are compelling.

Performance Statistics (Net of fees)

| | Celeste Australian Small Co. Fund | ASX Small Ord Acc Index | Performance | ASX Small Ind Acc Index | ASX Small Res Acc Index |
|---------------|---|-------------------------------|-------------|-------------------------------|-------------------------------|
| 1 month % | -3.8 | -2.8 | -1.0 | -3.2 | -1.1 |
| 1 year % | -4.4 | -7.4 | +3.0 | +7.8 | -42.6 |
| 3 years % pa | +2.2 | -6.2 | +8.4 | +7.0 | -30.6 |
| 5 years % pa | +16.7 | +8.6 | +8.1 | +14.0 | -4.3 |
| 10 years % pa | +10.0 | +4.8 | +5.2 | +5.8 | +2.9 |

Past performance is not necessarily indicative of future returns.

Fund at a Glance

Fund Information

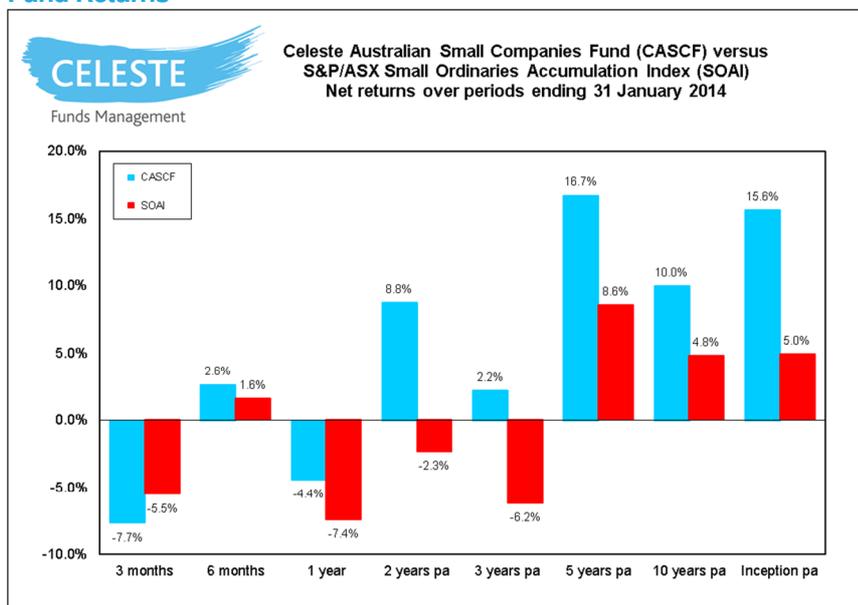
| | |
|--|---|
| Primary Investments | Shares in listed Australian smaller companies |
| Investment objective | Small Ordinaries Acc Index + 5% p.a. over rolling 3 years |
| Unit price (redemption) as at 31.01.2014 | \$3.0502 |
| Unit price (application) as at 31.01.2014 | \$3.0687 |
| Fund Size as at 31.01.2014 | \$192m |
| Minimum investment | \$25,000 |
| Minimum additional investment | \$1,000 |
| Minimum balance | \$15,000 |
| Minimum investment: monthly investment plan | \$500 |
| Redemption will generally be available in | 7 days |
| Distributions | 30 June and 31 December |
| Entry fee* | 0% |
| Exit fee* | 0% |
| Buy/Sell differential* | 0.30% |
| Management fee* | 0.95% |
| Performance fee** | 20% of return above benchmark |
| OGFM*** | 0.95% p.a. |

* These fees and charges apply for the duration of the Product Disclosure Statement (PDS) and are inclusive of the Goods and Services Tax.

** A fee charged on performance of the investments of the Fund above the nominated benchmark performance. The benchmark is the S&P/ASX Small Ordinaries Accumulation Index.

*** The Ongoing Fee Measure (OGFM) is the total amount of the ongoing Manager and Custodian Fees and aggregate Fund expenses in a Financial Year (but excluding the performance fee), divided by the average Net Asset Value of the Fund for the Financial Year expressed as a percentage. Transactional costs, such as bank charges, brokerage and stamp duties are not included in the ratio. The OGFM for the Fund will not exceed 0.95% p.a. for the duration of the PDS.

Fund Returns



Distribution History

| Total distribution year ended | Cents Per Unit | Annual Yield %* |
|-------------------------------|----------------|-----------------|
| June 99 | 3.07 | 2.9 |
| June 00 | 17.37 | 11.3 |
| June 01 | 13.88 | 7.8 |
| June 02 | 27.17 | 14.2 |
| June 03 | 7.01 | 3.9 |
| June 04 | 21.71 | 11.2 |
| June 05 | 49.48 | 19.5 |
| June 06 | 18.88 | 7.3 |
| June 07 | 34.32 | 12.3 |
| June 08 | 38.82 | 9.9 |
| June 09 | 10.06 | 4.2 |
| June 10 | 18.70 | 8.9 |
| June 11 | 11.89 | 4.6 |
| June 12 | 4.07 | 1.4 |
| June 13 | 15.81 | 5.5 |

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*CPU/unit price at beginning of period.

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Celeste Funds Management Limited

Level 14, 15 Castlereagh Street, Sydney NSW 2000. GPO Box 4266, Sydney NSW 2001

T 02 9216 1800 F 02 9216 1899 E contact@celestefunds.com.au

www.celestefunds.com.au