

Celeste Australian Small Companies Fund

Monthly update 31 May 2016

Performance Statistics (Net of fees)

	1 mth %	1 yr %	3 yrs % p.a.	5 yrs % p.a.	10 yrs % p.a.
Celeste Aust. Small Co. Fund	-0.6	+3.6	+1.0	+1.1	+5.3
Performance (relative to Index)	-4.7	-3.3	-5.9	+0.9	+4.0
S&P/ASX Small Ords Acc Index	+4.1	+6.9	+6.9	+0.2	+1.3
S&P/ASX Small Inds Acc Index	+4.8	+8.7	+10.8	+9.6	+3.7
S&P/ASX Small Res Acc Index	+0.8	-1.8	-8.3	-21.2	-5.6

Past performance is not necessarily indicative of future returns.

The Fund fell 0.6% in May, with its benchmark, the S&P/ ASX Small Ordinaries Accumulation Index increasing by 4.1%. Since inception (May 1998) the Fund's return is 13.3% pa, net of all fees, against the Index's 5.3% pa.

Portfolio Commentary

Nick Scali (NCK) increased 10.3% in May after announcing an upgrade to earnings expectations for FY16. Net Profit After Tax is expected to be between \$24m and \$26m, which was \$1.3m above market expectations and c.45% above FY15 NPAT of \$17m.

Lycopodium (LYL) rose 35.5% during the month after providing an earnings update for FY16. LYL expects an FY16 net profit of at least \$3m, on revenues of \$126m, compared to net earnings of only \$545,000, in H1. LYL is a best of breed WA based engineer and project management consultancy, and we remain attracted to the return profile and operational leverage LYL offers.

RCR Limited (RCR) increased by 21.4% during the month after the announcement of a number of new contracts awards, with a cumulative value of \$238m. The contracts announced in May underpin RCR's revenue pipeline into FY17, with the company likely to see significant earnings growth, year on year.

SAI Global (SAI) declined by 4.7% in May post updated earnings guidance for FY16. A slightly stronger \$A and ongoing softer performance in the European assurance business has seen the company trim FY16 expectations by 5%. Ongoing negotiations with Standards Australia and property settlement volumes continue to cloud SAI sentiment. Taking as given the lower earnings trajectory from these businesses, SAI looks oversold.

ClearView Wealth (CVW) declined by 1.6% over the month. Importantly CVW raised \$50m in new equity to repay bank debt and fund the growth of the business. CVW's advised life insurance new business is up 20% for the 10 months of FY16, funds under management are up 8% with increased advisor count and ongoing approved product list penetration. Importantly, underlying net profit for FY16 is expected to rise by 30-35%, with a final fully franked dividend of 2.5 cps. The company also announced that a pending strategic review of CVW, by the Board and Management, may see a change in control of CVW occur during H2 of FY16.

Portfolio Top 5 Holdings

Stock	% of Fund
1 REECE LIMITED	8.0
2 AMA GROUP	5.1
3 BREVILLE GROUP	5.0
4 STEADFAST GROUP	4.6
5 REGIS HEALTHCARE	4.5

Global Index Performance (Accumulation)

	1 month %	1 year %	3 years % pa
Australia – S&P/ASX All Ordinaries	+3.1	-1.2	+7.8
USA – S&P 500	+1.5	-0.5	+10.1
USA – NASDAQ Composite	+3.6	-2.4	+14.8
Europe – FTSE (UK)	-0.2	-10.8	-0.9
Europe – DAX (Germany)	+2.2	-10.1	+9.6
Asia – Nikkei (Japan)	+3.4	-16.2	+11.6
Asia – Shanghai Composite (China)	-0.7	-36.8	+9.3

Monthly Commentary

Global equity markets fell in the first few weeks of May but rallied strongly into the month end. Mining and energy stocks were sold off, stocks on premium multiples garnered further investor interest and Government long bond yields globally edged lower.

At the start of May the Reserve Bank of Australia (RBA) cut the official cash rate to a record low of 1.75%, which saw the 10 year yield move to 2.23%. The Australian long bond rate compares with a US 10Y bond rate of 1.85%, a Spanish 10Y bond rate of 1.47%, and an Italian 10Y bond rate of 1.36%. Interestingly the payback period for these international gilts is 54 years for the US 10Y bond, 68 years for the Spanish 10Y bond and 74 years for the Italian 10Y bond.

The RBA's May Statement on Monetary Policy downgraded its long term expectation of inflation, increasing the probability of further cuts to the cash rate over calendar 2016. The RBA's policy statement forecast that underlying inflation will be some 1% lower, over the year to December 2016, compared to their forecast in Feb. 2016, and that in the medium term, to mid-2018, underlying inflation will stay at the bottom end of their 2% - 3% forecast range. On the domestic economic front the unemployment rate was 5.7%, the equal lowest since September 2013. The wage price index for Q1 of CY16 rose 0.4%, quarter on quarter, or 2.1% year on year, a record low since the data series started in 1991. The March quarter CPI came in at -0.2% quarter on quarter, taking the annual inflation rate to 1.3% year on year, the lowest rate seen in 17 years.

In the USA, the unemployment rate remained steady at 5%, industrial production in April grew at a better than expected 0.7%, month on month, whilst Q1 GDP was revised to 0.8% quarter on quarter. In Q1, consumer spending grew at a rate of 1.9%, with the consumer accounting for over 2/3 of the US economy. Investor sensitivity to US interest rate movement remains high with a stronger economic outlook providing the appropriate backdrop for further rate hikes in coming months.

Economic data from China in April included retail sales growth of 10.1% year on year, fixed asset investment rose 10.5%, whilst industrial production was up 6.0%. Despite a slowing economy, employment data remains stable with 13.1m Chinese urban jobs created in 2015, and registered urban-unemployment at 4.05%.

In the coming months we expect that the economic backdrop will remain sombre and that generating earnings growth will remain problematic. At Celeste we remain sensitive to the pricing of risk, current lofty valuations in the equity market, and the lack of overt risk and reward sensitivity. Celeste retains its patient investment disposition, a process centric mindset, and an eye on tax effective medium to longer term returns.

CELESTE

Funds Management

Fund at a Glance

Fund Information

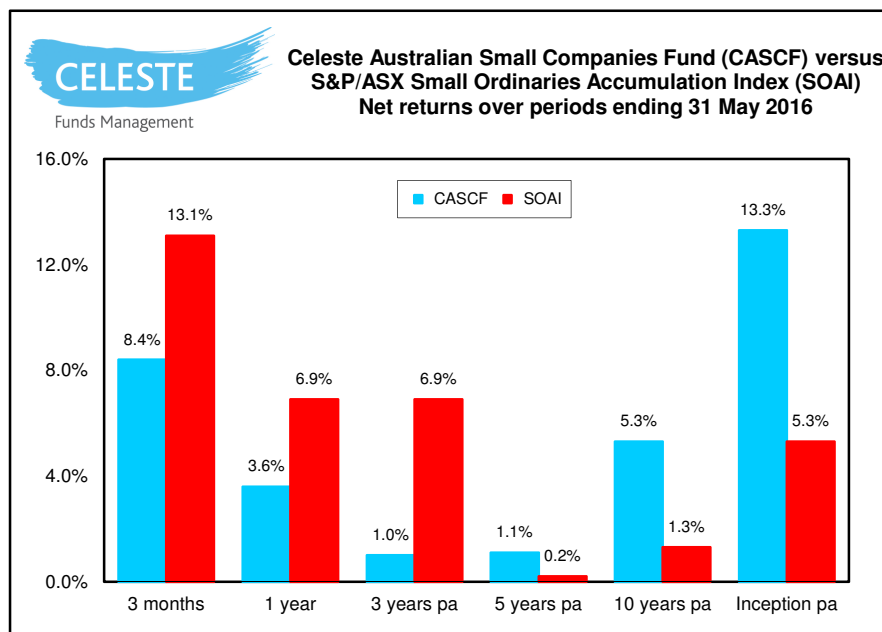
Primary Investments	Shares in listed Australian smaller companies
Investment objective	Small Ordinaries Acc Index + 5% p.a. over rolling 3 years
Unit price (redemption) as at 31.05.2016	\$2.6748
Unit price (application) as at 31.05.2016	\$2.6910
Fund Size as at 31.05.2016	\$69m
Minimum investment	\$25,000
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 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
June 14	14.56	5.4
June 15	12.67	4.5

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* CPU / unit price at beginning of period

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