

## Celeste Australian Small Companies Fund

Monthly update 31 August 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	+8.7	+27.7	+4.2	+6.2	+6.6
Performance (relative to Index)	+10.3	+1.2	-2.9	+3.6	+5.2
S&P/ASX Small Ords Acc Index	-1.6	+26.5	+7.1	+2.6	+1.4
S&P/ASX Small Incls Acc Index	-0.5	+22.4	+10.6	+11.7	+3.6
S&P/ASX Small Res Acc Index	-6.2	+48.7	-6.6	-18.2	-4.9

Past performance is not necessarily indicative of future returns.

The Fund rose 8.7% in August, with its benchmark, the S&P/ASX Small Ordinaries Accumulation Index decreasing by 1.6%. Since inception (May 1998) the Fund's return is 14.2% pa, net of all fees, against the Index's 5.5% pa.

### Portfolio Commentary

**Cleanaway Waste Management (CWY)** rose 32.2% during the month after reporting a FY16 result that exceeded market expectations. Underlying EBITDA of \$281.3m was up 21.6% on last financial year, although this included the annualised benefit of a significant landfill acquisition. New management has improved CWY waste collection volumes with net customer churn now positive for the first time in years. CWY has also initiated a major rationalisation program that delivered significant cost and cash flow savings in FY16, with further benefits anticipated in FY17 and FY18.

**Reece Limited (REH)** rose 15.6% during August and reported a very strong FY16 result. Sales in FY16 grew 9.2%, EBITDA was up 18.5%, whilst ROCE was 31.9%. The REH competitive position remains strong, and the group should benefit from any improvement in housing renovation activity, an area where spend has been quite muted in recent times. REH remains well placed, with sales, earnings and returns to shareholders set to grow in the medium term.

WA based engineering consultancy, **Lycopodium Limited (LYL)** was up 40.2% in the month after delivering a solid FY16 result and guiding to a significantly improved FY17. LYL management expect that based on current work in hand the company will see revenues grow to over \$200m in FY17, compared to FY16's \$124m. With the growth in revenue anticipated in FY17, LYL expect that NPAT will grow some 60% from \$3.8m to \$6m. We remain attracted to the track record, conservatism and operational leverage offered.

**Regis Healthcare (REG)** declined by 11.2% over the month despite reporting a 24% increase in NPAT, and guiding to at least 15% earnings growth in FY17. REG has a strong pipeline of new facilities that are set to deliver additional aged care places supporting further revenue & earnings growth beyond 2020. We remain comfortable with the positioning of REG, its management team and the long term opportunity in the aged care sector.

### Portfolio Top 5 Holdings

Stock	% of Fund
1 REECE LIMITED	7.2
2 AMA GROUP	4.9
3 BREVILLE GROUP	4.7
4 RCR TOMLINSON	4.6
5 IMF BENTHAM	4.4

### Global Index Performance (Accumulation)

	1 month %	1 year %	3 years % pa
Australia – S&P/ASX All Ordinaries	-1.3	+10.7	+7.1
USA – S&P 500	-0.1	+10.1	+10.0
USA – NASDAQ Composite	+1.0	+9.1	+13.2
Europe – FTSE (UK)	+0.8	+8.5	+1.9
Europe – DAX (Germany)	+2.5	+3.2	+9.3
Asia – Nikkei (Japan)	+1.9	-10.6	+8.0
Asia – Shanghai Composite (China)	+3.6	-3.8	+13.7

### Monthly Commentary

August was a volatile month for local equities with a year to date high for the All Ords. Index on August 1<sup>st</sup>, before an end of month sell off. The Aug. end, risk off move, was fuelled by Janet Yellen, US Fed Reserve Governor, stating that "...the case for an increase in the federal funds rate has strengthened in recent months..."

Globally, bond yields remain at historic lows with the US 10 year bond trading at a yield of 1.59%. Surprisingly, fiscally challenged European countries are also seeing historically low bond rates with Spanish and Italian 10 year bonds trading on yields of 1.01% and 1.14%, respectively. Given the return characteristics of these debt instruments, with paybacks of 70 to 100 years, an element of risk mispricing does appear to be evident.

A combination of low inflation and low wages growth led the Reserve Bank of Australia to lower the cash rate by 25 basis points to 1.5% on 3 August. The commercial banks failed to pass on the full rate cut to customers, blunting the stimulatory effects of this move. Locally, we saw a spike in July residential building approvals, up 11.3% month on month, to a near record high of 252,000. While building approvals were strong, wage growth in Australia remains very weak at +0.5% in the second quarter of 2016. Year on year wages growth is just 2.1%, well below the long run average of 3.5%.

In early August, UK official interest rates were cut from 0.5% to a nominal 0.25%. The Bank of England also signalled that rates could go even lower if the economy worsens.

In a rare piece of good news for the Japanese economy, the unemployment rate fell to 3% in July, the lowest for 21 years. The Japanese economy grew just 0.2%, in the three months to June, with the Japanese cabinet approving yet another stimulus package worth more than 28 trillion yen (US\$275 billion). During August, the Governor of the Bank of Japan, Haruhiko Kuroda noted that, "...the zero lower bound of nominal interest rates is no longer an insurmountable constraint in practice...". During the month, the Japanese yield curve moved further into negative territory with the 20 year bond negative for the first time, and the yield on the 30 year bond down to 0.15%.

August reporting season gave investors little basis for optimism with companies citing an anaemic revenue environment, ongoing cost pressures, and delivery of earnings growth a challenge. Given current lofty equity market valuations and little earnings growth evident, we expect that equities will remain choppy in coming months. At Celeste, we remain process centric, aware of risk and reward factors and alert to taking opportunities that the market presents us.

## Fund at a Glance

### Fund Information

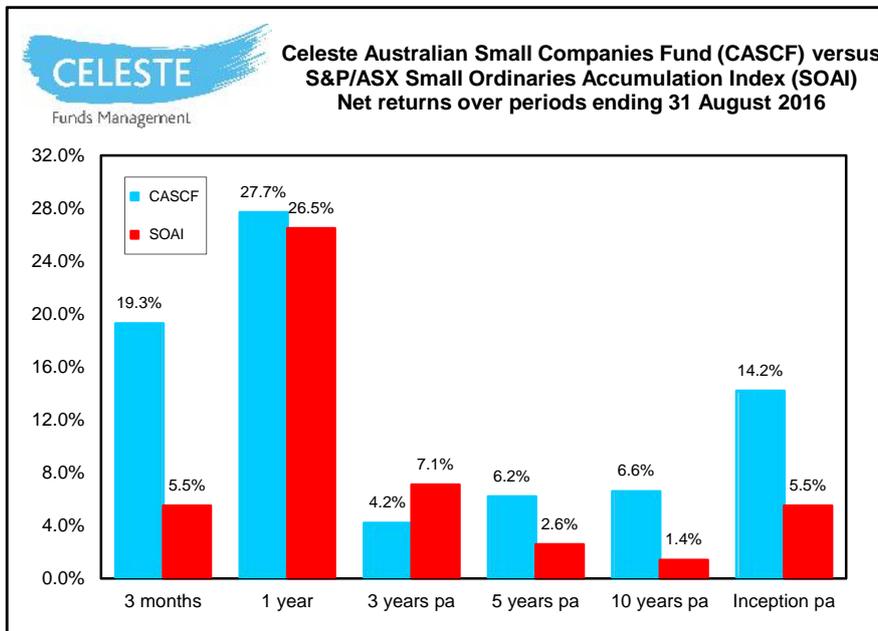
<b>Primary Investments</b>	Shares in listed Australian smaller companies
<b>Investment objective</b>	Small Ordinaries Acc Index + 5% p.a. over rolling 3 years
<b>Unit price (redemption) as at 31.08.2016</b>	\$3.1211
<b>Unit price (application) as at 31.08.2016</b>	\$3.1400
<b>Fund Size as at 31.08.2016</b>	\$63m
<b>Minimum investment</b>	\$25,000
<b>Minimum additional investment</b>	\$1,000
<b>Minimum balance</b>	\$15,000
<b>Minimum investment: monthly investment plan</b>	\$500
<b>Redemption will generally be available in</b>	7 days
<b>Distributions</b>	30 June and 31 December
<b>Entry fee*</b>	0%
<b>Exit fee*</b>	0%
<b>Buy/Sell differential*</b>	0.30%
<b>Management fee*</b>	0.95%
<b>Performance fee**</b>	20% of return above benchmark
<b>OGFM***</b>	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



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### Distribution History

Total distribution year ended	Cents Per Unit	Annual Yield %*
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
June 16	9.95	4.0

\* CPU / unit price at beginning of period

This report is intended to provide only general securities advice. Celeste Funds Management Limited does not purport to make any recommendation that any securities transaction is appropriate to your particular investment objectives, financial situation or particular needs. Prior to making any investment decision, you should assess, or seek advice from your adviser, on whether any relevant part of this report is appropriate to your individual circumstances. Celeste Funds Management Limited believes that the information contained in this report has been obtained from sources that are accurate, but it has not checked or verified that information. Except to the extent that liability cannot be excluded, Celeste Funds Management Limited accepts no liability for any losses or damage caused by any error in or omission from this report

### 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](mailto:contact@celestefunds.com.au)

[www.celestefunds.com.au](http://www.celestefunds.com.au)

ABN 78 098 628 605