Perennial Socially Responsive Shares Trust

PERENNIAL GROWTH MANAGEMENT

Monthly Report
30 June 2015

	Month	Quarter	FYTD	1 year	2 years	3 years	5 years
	%	%	%	%	% p.a.	% p.a.	% p.a.
Perennial Socially Responsive Shares Trust*	-5.3	-5.5	4.3	4.3	13.1	15.5	8.8
S&P/ASX 300 Accumulation Index	-5.3	-6.5	5.6	5.6	11.3	14.7	9.5
Value Added (Detracted)	**0.0**	**1.0**	**-1.3**	**-1.3**	**1.8**	**0.8**	**-0.7**
Net Performance	-5.4	-5.8	3.3	3.3	12.1	14.4	7.7

* Gross Performance. Past performance is not a reliable indicator of future performance.

Perennial Socially Responsive Shares Trust

The Trust aims to provide a total return (after fees) that exceeds the S&P/ASX 300 Accumulation Index measured on a rolling three-year basis, by investing in a selection of listed companies which also embrace and engender social performance in their corporate culture.

Portfolio manager:
Lee Mickelburough

Risk profile:
High

Trust FUM (as at 30 June 2015):
AUD51.1 million

Income distribution frequency:
Half yearly

Team FUM (as at 30 June 2015):
AUD2.5 billion

Minimum initial investment:
$25,000

Trust inception date:
December 2001

APIR code:
IOF0117AU

- **The Australian market fell 5.3% in June and for the second month in a row underperformed most of its global peers.**
- **Stocks held that contributed most to portfolio performance during the month were James Hardie and Infigen Energy while the key detractors were Fairfax Media and SEEK.**
- **The portfolio increased its holdings in Caltex and Orocobre, and exited its holding in Goodman Group.**

Trust performance overview

The Perennial Socially Responsible Shares Trust (the Trust) performed in line with the S&P/ASX300 Accumulation Index (the Index) in June, finishing down 5.3% against the Index which finished down 5.3% for the month.

At a sector level, Telco's finished down yet still outperformed in June (down 1.3%) as did Financials (down 2.8%). All other sectors underperformed the market with Materials (down 8.3%) and Consumer Discretionary (down 10.9%) the worst performing sectors. Healthcare (down 5.8%), Utilities (down 6.1%), Energy (down 7.8%), Industrials (down 7.7%) and Consumer Staples (down 7.8%) were also underperformers.

Investment Themes and Stock Performance

Companies which possess strong fundamentals for growth will continue to outperform.

Despite a strong performance following the delivery of a Domain business update in late March, and trading update in early May, **Fairfax Media Limited (overweight, down 20.9%)** underperformed in June on little company specific news. In May management noted Domain Digital sales were up 32% and overall Domain sales were up 54% (including acquisitions), this was above market expectations; however they also pointed to higher costs as they reinvest across the Group. A depreciation in the New Zealand dollar in recent months has also been a drag on Fairfax earnings, with New Zealand generating over 20% of profits, explaining some of the recent weakness. We believe Domain is well positioned to grow its business and disrupt market leader REA, offering a credible and affordable alternative online distribution channel for the property sector.

We reduced our position in **Regis Healthcare Limited (overweight, down 9.3%)** after a period of strong outperformance. While we remained attracted to the company's growth prospects through the consolidation of the industry, in our view, the elevated share price left no room for earnings disappointment from Regis or its industry peers. Recent industry research has pointed to preference for lump sum accommodation payments (RADs) rather than daily payments (DAPs) under the newly introduced funding model. While delivering a similar economic outcome, the implication of the higher than expected proportion of RADs is positive for cash flow but negative for accounting profits. This could leave analyst earnings estimates for the sector vulnerable to disappointment at the upcoming results season, and was a likely contributor to the sharp sell-off in the sector late in June.

We continued to trim our position in **SAI Global Limited (overweight, down 6.3%)** after a period of outperformance. The rally in SAI Global shares was driven by the company announcement that it is entering a managed services agreement with HCL Australia Services to outsource a number of its IT related functions. SAI management expects the agreement to create approximately $27m in savings over the five year deal.

We added to our position in **Caltex (overweight, down 5.5%)** in June, taking advantage of a period of weaker share price performance. Chevron's exit from the register in March remains significant as the probability of liberating the $1.1b of excess franking credits that sit on Caltex's balance sheet is increased. Following the closure of the Kurnell refinery late last year (which has reduced earnings volatility and freed up substantial working capital) Caltex is arguably under geared and well-placed to either materially increase dividends or undertake off market share buybacks to distribute franking credits. Caltex has an improving growth outlook, boosted by a company-wide cost out program which will deliver up to 10% earnings upside by FY16 and Fuel Retailing is assisted by the ACCC's decision to limit supermarket fuel discounts at 4 cents per litre.

We increased our position in **Orocobre Limited (overweight, down 20.2%)** during the month as the company implemented a $32m capital raising at $1.90 per share. Prior to the capital raising we took the opportunity to visit the mine site in Argentina and came away comfortable that, despite the slower than expected ramp up and requirement for more remedial capital expenditure than initially believed, this capital raising will see them through commissioning and achievement of nameplate capacity by year end. We note that the lithium market remains tight with the expected supply response disappointing relative to expectations and as such realised prices have increased 10-15% this year.

The economic recovery in the US continues as evidenced by generally supportive economic data.

This remains a central theme in our portfolio construction. We are seeing the gradual normalisation of US monetary policy, ongoing recovery in the USD dollar and general upward pressure on US interest rates. We have chosen to play this central theme through tilting the portfolio towards those companies that have operations whose fundamentals that will be supported in this environment.

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James Hardie Industries (overweight, up 1.9%) outperformed as macro conditions in particular in the US, remain supportive and management executes effectively on its growth targets. Input costs have been declining with freight, pulp and gas all down over the last 12 months. James Hardie's manufacturing facilities have also been more productive with volumes strong in FY15, with management confident the sustainability of manufacturing performance can be maintained going forward. They have been taking share from US vinyl manufacturers and are looking to capitalise on this growth going forward by increasing sales capability in the US. We remain attracted to the strong market position, clear strategy and see valuation upside from current levels.

In recent months we have been reducing the portfolio's position in Goodman Group (exited) despite it's global appeal, as the stock approached valuation after a period of strong outperformance, and this sale was completed in June.

Chinese economic data has remained underwhelming.

The Chinese leadership face the reality of balancing long term reforms on corruption, the environment and market liberalisation with maintaining economic growth. Despite the weaker growth we had previously not observed any significant changes of government policy; consistent with our view that the leaders are maintaining a long term view of China's growth trajectory

There are signs that the Chinese government is becoming more aggressive in their management of the economy, the Peoples Bank of China (PBOC) announced its fourth interest rate cut in seven months, cutting the one year benchmark rate another 25 basis points to 4.85% and the benchmark deposit rate to 2.0%. The reserve requirement ratio for banks' lending to farmers and small businesses was reduced by 50 basis points. We feel these moves may signify the government is becoming more concerned about the state of growth in the Chinese economy. In this light we feel that it is reasonable to maintain our cautious approach in relation to companies with direct exposure to China.

Concerns over the sanctity of **Origin Energy's (not held, down 10.1%)** APLNG's offtake agreement with its 25% equity holder and largest offtaker, Sinopec weighed heavily on the stock late in the month. The timing of commencement of the signed offtake agreements is important for Origin as it ultimately determines when the cash flows will be available to start deleveraging their balance sheet. Balance sheet leverage is the key investment issue for this stock as we can see there is valuation support and cash flow growth.

BHP Billiton Limited (not held, restricted, down 8.6%) also underperformed the market during the month as commodity prices continued to weaken and concerns arose regarding future growth from the petroleum division. While we believe that there is little risk to BHP's progressive dividend we would note that this is likely to come at the expense of growth capital expenditure thereby raising questions about the long term growth rates implied in the current BHP share price.

During the month we reduced our position in **Western Areas Limited (overweight, down 9.5%)** on the back of stronger share prices early in the month relative to underlying nickel prices which continued to deteriorate. Late in the month Western Areas announced that they had bought Cosmos nickel operation from Glencore for A$24m. We view this acquisition as opportunistic, providing Western Areas with a cheap option on both the nickel price and exploration around this asset. We believe that Western Areas is a well-run company with a clean balance sheet that generates cash even at current nickel prices.

A lower oil price, down 4% in the month, weighed on **Karoon Gas Australia Limited (overweight, down 18.2%)** while delays to the start of drilling at the Levitt-1 exploration well meant that exploration news flow was limited. This well is a material event for Karoon, targeting a net unrisked prospective resource best estimate of 110 million barrels. During the month Karoon's joint venture partner in the well, Apache, finalised the sale of their Australian subsidiary to Macquarie Capital Group Limited and Brookfield Asset Management Inc. Karoon waived their pre-emptive rights over the 50% interest in the permit as a result of the Change in Control provisions in the joint operating agreement as Macquarie Capital Group Limited and Brookfield Asset Management Inc. have placed a value of US$241m on their 50% interest in the permit.

At the close of the month the Trust held 38 stocks and had an effective cash balance of 4.3%.

Market Overview

The Australian market fell 5.3% on an accumulated basis in June and for the second month in a row, underperformed most of its global peers. Markets were weak globally; the S&P 500 declined 2.1%, the Dow Jones fell 2.2% and the NASDAQ also fell, albeit a lesser 1.6%. European markets were weak with the Euro Stoxx 50 down 4.1% and the FTSE 100 declining 6.6%. Asian markets followed the trend with the Nikkei 225 the best performer falling only 1.6%. The Shanghai Composite fell 7.4%, while the Hang Seng Index returned a comparatively better result of - 4.3%.

The S&P 500 experienced a relatively quiet month up until the end of June when concerns emerged over the ongoing participation of Greece in the Eurozone bailout program. The US Fed's June FOMC meeting suggested to the market that the timing of the first interest rate rise may be further out than the market had previously expected. In the process, Fed officials lowered economic growth forecasts for 2015 to a range of 1.8%-2.0% from the previous estimation of 2.3%-2.7%. Following finding a base last month, the ISM manufacturing PMI rose to a five month high of 52.8, ahead of the the March and April readings of 51.5, and ahead of the 52.0 expected. By contrast, the ISM non-manufacturing PMI fell significantly to 55.7, well below the April reading of 57.8 and the 57.0 expected. The Thomson Reuters/University of Michigan consumer confidence index rose to 96.1, ahead of the previous reading of 95.9 and ahead of the 94.6 reading expected. Non-farm payrolls climbed from 223,000 in April to register a reading of 280,000 in May, well ahead of the 226,000 expected. The participation rate rose 0.1% to 62.9% while the US unemployment rate crept up to 5.5% in May from 5.4% in April, 0.1% higher than expectations. Housing starts slumped 11.1% in May after soaring 20.2% for the month of April - volatility in the series remains high. Building permits climbed 11.8% significantly ahead of the 3.5% decline expected. Core CPI for May rose 0.1% for the month, just lower than the 0.2% expected.

Chinese economic data remained patchy and the PBOC announced its fourth interest rate cut in seven months, cutting the one year benchmark rate another 25 basis points to 4.85% and the benchmark deposit rate to 2.0%. The reserve requirement ratio for banks with lending to farmers and small businesses was reduced by 50 basis points. The HSBC Flash Manufacturing PMI was stronger than the market had forecast coming in at 49.6, compared to the 49.4 expected and ahead of the revised April number of 49.2. May M2 money supply growth increased to 10.6% year on year from April's reading of 10.1%, below the 10.4% expected. New loan creation came in at 900.8B Yuan for May ahead of the 850B Yuan expected, yet behind April's 1050B Yuan number.

As was widely expected, the RBA kept the benchmark rate steady at 2.0% in June. Of note, the RBA stated that further depreciation of the Australia dollar seemed "both likely and necessary". NAB business confidence leapt up to 7 points in May from a reading of 3 points in April. The NAB business conditions rose 3 points to a reading of 7 for the same period. The Westpac MI consumer confidence sank to 95.3 in June from a reading of 102.4 in May. The economy gained 42,000 jobs in the month of May well ahead of the the 15,000 increase forecast, while the participation rate stayed steady at 64.7%. The unemployment rate unexpectedly declined to 5.96% a 0.24% decrease on the prior reading. As we have mentioned previously, the ABS figures in respect to unemployment figures have been volatile since the ABS changed sampling techniques and caution should be taken in reading too much into this data. Retail sales growth was flat in April, behind the 0.5% rise expected and the 0.3% increase in the prior period. Building approvals declined 4.4% in the month of April, ahead of the 1.8% decline expected.

The Australian dollar remained relatively stable against the US dollar in June, rising 0.3c. The US dollar traded relatively weaker against most currencies as the comments made at the FOMC tempered expectations of an interest rate hike in the near term. Somewhat surprisingly, the Australian dollar fell against the Euro despite the ructions in the European Monetary Union caused by the potential exit of Greece.

In bond markets, global government long bond yields rose during the first half of the month before partially retracing during the second half of the month on rising risk aversion as the drama of the Greek sovereign debt crisis played out and the Chinese stock market began to crater after reaching incredibly buoyant valuation metrics. The benchmark 10-year yield for Australia finished up 28 basis points for the month.

Spot Brent crude oil experienced a second month of declines, falling 4.0% in June. Iron ore followed suit with a matching decline of 4.0%. Base metals experienced a second particularly difficult month in June, with tin and lead the worst effected, both falling close to 10%. Spot gold fell 1.5% despite the ongoing uncertainty of a potential Greek exit from the Eurozone.

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Best/Worst Performers			
(Best) company	Month Return	**(Worst) company**	Month Return
BHP Billiton Limited (restricted) (not held)	-8.6	Seek Limited	-16.9
Wesfarmers Limited (not held)	-10.6	Fairfax Media Limited	-20.9
James Hardie Industries PLC	1.9	Mayne Pharma Group Limited	-12.8
Asciano Limited	-1.6	Karoon Gas Australia Ltd	-18.2

New/Increased positions	
Caltex Australia	Increased
Orocobre Limited	Increased

Exited/Decreased positions	
Goodman Group	Exited
SAI Global Limited	Reduced
Seek Limited	Reduced
Western Areas Ltd	Reduced

Top 10 Holdings		
Stock name	Trust weight %	Index weight %
ANZ Banking Grp Ltd	9.1	6.3
Westpac Banking Corp	8.9	7.1
National Aust. Bank	7.4	6.2
Commonwealth Bank.	6.9	9.8
Caltex Australia	4.0	0.6
Macquarie Group Ltd	3.7	1.9
Asciano Limited	3.5	0.5
AMP Limited	3.2	1.3
Westfield Corp	3.2	1.2
Challenger Limited	3.0	0.3

Asset Allocation		
Sector	Trust weight %	Index weight %
Energy	6.1	5.1
Materials	10.9	14.8
Industrials	10.5	7.2
Consumer Discretionary	4.5	4.3
Consumer Staples	0.0	6.5
Healthcare	7.3	6.0
Financials-x-Real Estate	45.0	39.2
Real Estate	3.2	7.9
Information Technology	0.0	1.0
Telecommunication Services	2.5	5.9
Utilities	2.7	2.0
Cash	7.2	-

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