Perennial Value Shares for Income Trust

Quarterly Report
31 December 2014

	Quarter	FYTD	1 year	3 years	5 years	Since Inception^
	%	%	%	% p.a.	% p.a.	% p.a.
Perennial Value Shares for Income Trust*	3.2	4.2	7.8	18.4	9.1	7.6
S&P/ASX 300 Accumulation Index	2.9	2.4	5.3	14.7	6.5	5.8
Value Added (Detracted)	**0.3**	**1.8**	**2.5**	**3.7**	**2.6**	**1.8**
Capital Growth	1.5	0.6	2.2	12.3	3.4	1.4
Income Distribution	1.5	3.2	4.7	5.1	4.9	5.4
Net Performance^^	3.0	3.8	6.9	17.4	8.3	6.8

*Gross Performance. ^Since inception: December 2005. ^^This refers to the Trust's gross performance net of investment management fees. Past performance is not a reliable indicator of future performance.

Perennial Value Shares for Income Trust

The Trust aims to provide investors with an attractive level of tax effective income, which the Trust aims to pay via quarterly distributions. The Trust aims to provide a dividend yield, adjusted for applicable franking credits and before fees, above that provided by the S&P/ASX 300 Accumulation Index*.

Portfolio manager:
Stephen Bruce

Risk profile:
High

Trust FUM (as at 31 December 2014):
AUD71.7 million

Income distribution frequency:
Quarterly

Team FUM (as at 31 December 2014):
AUD7.4 billion

Minimum initial investment:
$25,000

Trust inception date:
December 2005

APIR code:
IOF0078AU

*Gross dividend yield.

- **A pre-tax distribution yield for the last 12 months of 6.6%.**
- **The better performing sectors over the quarter tended to be the defensives.**
- **Stocks with significant offshore earnings tended to outperform, rallying on the lower AUD.**

Trust Characteristics

In line with the objective, the Trust continues to invest in a portfolio of financially sound companies which demonstrates superior dividend yield characteristics to the overall stock market.

Quarterly Distribution

The Trust paid a distribution of 1.7 cents per unit for the December quarter. Adding franking credits, the gross (pre-tax) distribution for the quarter was 2.5 cents per unit. Based on the unit price at the start of the financial year ($1.15), this represents a pre-tax distribution yield for the quarter of 2.1% and brings the pre-tax distribution yield for the last 12 months to 6.6%. This compares favourably to the 12 month term deposit rates available for that period of around 3.4%.

Portfolio Activity

During the quarter we took profits and reduced our holdings in a number of stocks which had performed strongly over the past 12 months. These included Amalgamated Holdings, Aristocrat Leisure, Amcor, Harvey Norman, Lead Lease, Suncorp, Telstra and Westfield Corporation. We also exited our holding in Brambles entirely as it had become very expensive. At our selling price of $9.21, the stock no longer represented attractive value, with an FY15 P/E of 18.6x and gross yield of only 3.8%.

Proceeds were used to increase our holdings in ANZ, NAB and Westpac. While some uncertainty remains over ultimate impacts on the sector from the Financial System Inquiry, the banks are fundamentally in good shape and offer a sector average FY15 gross yield of 8.1%. We also increased our holding in Macquarie Group, which will be benefitting from strong asset prices in its infrastructure and funds management businesses and increased volatility in its commodities business. During the quarter, we added Rio Tinto to the portfolio. As a major producer of iron ore, positioned at the bottom of the global cost curve, this company is set to generate strong earnings, even at the current relatively low iron ore prices.

The portfolio remains well diversified, with exposures to a range of industries, with holdings across eight sectors. At quarter end, stock numbers were 26 and cash was 3.3%.

Stock and Portfolio Performance

The benchmark S&P/ASX 300 Accumulation Index (the Index) finished the quarter up 2.9%. The Perennial Shares for Income Trust (the Trust) finished the quarter up 3.2%, outperforming the Index by 0.3%. For calendar year 2014, the Trust has delivered a total return of 7.8%, outperforming the Index by 2.5%.

Global markets finished a volatile December quarter mixed, with the S&P500 (up 4.4%) and Nikkei 225 (up 7.9%) up, while the FTSE 100 (down 0.9%) and Euro Stoxx 50 (down 2.5%) declined. The major event during the quarter was the sharp decline in oil prices, which undermined confidence in the global economy as well as impacting the share prices of energy producers. However, there was further evidence that global growth is improving. In particular, the data for the US was positive, with the revised Q3 GDP data showing the firmest rate of growth since 2003 and non-farm payrolls growing 321,000, well above expectations. In other regions, key German data improved, there were positive signs that Japan's economy is emerging from recession in the current quarter and China's data was consistent with a growth rate close to 7% in Q4, although a key manufacturing PMI dropped below 50. Global inflation continued to fall suggesting a prolonged period of low interest rates.

In Australia, GDP growth was unexpectedly weak in the September quarter, with real disposable income falling again, however, the partial data for the fourth quarter pointed to improvement. Retail sales for October were soft, albeit better than expected and home building approvals boomed, as did employment for November. The jobless rate, however, rose to a new 12-year high of 6.3%, and business and consumer sentiment fell, with the mid-year economic update revealing further deterioration in the budget deficit, largely due to lower commodity prices. The RBA left interest rates unchanged at 2.5% and the AUD continued to fall, reaching a four-year low of 81 US cents.

The better performing sectors over the quarter tended to be the defensives, with Healthcare (up 13.3%), Telcos (up 12.3%) and REITs (up 11.3%). Industrials (up 7.6%) and Financials (up 7.2%) also outperformed, while the cyclical sectors lagged, with Energy (down 17.7%) the worst performing sector, followed by Metals and Mining (down 10.9%) and Materials (down 6.1%).

Stocks with significant offshore earnings tended to outperform, rallying on the lower AUD. These included Westfield Corporation (up 21.1%), Amcor (up 19.9%) and Lend Lease (up 14.4%). Aristocrat Leisure (up 13.7%), another beneficiary of a weaker AUD, also delivered a strong full year result which demonstrated significant market share gains in its key US and Australian markets. As a major hotel operator, Amalgamated Holdings (up 12.3%) also stands to benefit from a lower AUD as this should both generate more inbound tourism and encourage more Australians to holiday domestically. Telstra (up 12.6%), rallied after signing the revised NBN deal.

Stocks which detracted from performance were predominantly our resource holdings, with Iluka Resources (down 24.3%), Origin Energy (down 22.0%), BHP (down 13.3%), Woodside Petroleum (down 6.4%) and Rio Tinto (down 2.7%).

ESG Factors during the quarter

Perennial Value Management remains alert to Environmental, Social and Corporate Governance (ES&G) issues in the portfolio. During the quarter, Orica reported that their greenhouse gas abatement program has seen a 50% reduction in nitrous oxide emissions from their manufacturing plants since 2010. This is the equivalent of taking over 300,000 cars off the road. In a separate initiative, Orica is a 40% stakeholder in Mineral Carbonation International. This is a collaboration between Orica, the NSW and Commonwealth Governments and the University of Newcastle to develop a new carbon capture and storage technology to be retrofitted to power stations. The technology is proven at laboratory scale and a pilot plant is to be constructed in early 2015. If successful, this has the potential to significantly reduce CO2 emissions.

Market Outlook

The December quarter highlighted the ongoing volatility in markets. However, investors should take comfort from the fact that the recent reporting season showed that company earnings are growing and valuations are reasonable. The fall in energy prices, if sustained should also provide further economic stimulus. Longer-term, as economic growth resumes and broadens, led in particular by a recovering US economy, company profits will continue to grow and dividends paid to shareholders will increase, providing a growing stream of reliable, tax-effective income to investors.

Top 10 Holdings		
Stock name	Trust weight %	Index weight %
Telstra Corporation.	9.5	5.3
National Aust. Bank	8.9	5.9
Westpac Banking Corp	8.8	7.5
ANZ Banking Grp Ltd	8.8	6.4
BHP Billiton Limited	7.9	6.9
Commonwealth Bank	5.8	10.1
Woodside Petroleum	5.6	2.0
Macquarie Group Ltd	4.9	1.4
AMP Limited	3.9	1.2
Suncorp Group Ltd	3.9	1.3

Asset Allocation		
Sector	Trust weight %	Index weight %
Energy	6.8	5.1
Materials	14.7	15.0
Industrials	1.0	7.4
Consumer Discretionary	7.0	4.1
Consumer Staples	2.0	7.4
Health Care	0.0	5.9
Financials-x-Real Estate	48.9	38.6
Real Estate	6.9	7.7
Information Technology	0.0	1.0
Telecommunication Services	9.5	5.8
Utilities	0.0	1.9
Other	3.3	-

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