

Perennial [partner] Professional's Pick – Flight Centre and Wealth Defender Equities

Posted By *Stephen Bruce* On 19/09/2016 @ 11:27am In | [Comments Disabled](#)

Stock: Flight Centre (ASX: FLT)

Flight Centre ticks a lot of boxes in terms of what we look for in an investment.

Strong balance sheet – The company is in an extremely strong financial position, with net cash of \$430 million as at 30 June 2016. A strong balance sheet is critical as it gives a company flexibility to pursue growth opportunities, enables a company to sustainably pay dividends and, importantly, limits the downside risk.

Strong market position – Flight Centre has a very strong market position, being the market leader in Australia, as well as having substantial offshore operations and serving both the retail and corporate market. Globally, the business operates around 3,000 branches, with 19,000 staff in 14 countries. This scale gives it purchasing power with airlines and accommodation providers.

Good management – This is critical! To this day, Flight Centre is still led by CEO Graham Turner, one of its founders and a major shareholder, owning around 15% of the company. We like companies with proven management, who deeply understand their industry and still have plenty of "skin in the game". It is this sort of management team that takes a longer-term view and builds a great business.

Track record of profitability – We like stocks with a proven track record, rather than just lots of "blue-sky" upside. This stock has been a great long-term performer, having delivered strong earnings growth since listing in 1995. This has been reflected in share price performance, with the stock generating a total return of 14.1% pa over the last 10 years.

Of course, simply liking a stock is not enough – it also has to be trading at a price that offers good value. We've held this stock several times in the past and most recently, have been increasing our position in May and June at a price of around \$31.80. At these levels, the stock looked great long-term value to us.

The FY16 result in August saw the stock rally, finishing the month up +14.5%. While earnings for the period were down slightly as a result of intense airfare competition (it's a good time to take a trip – return to the US for \$939!), we were pleased to see management continue to invest to roll out the global footprint, improve its online capabilities and launch new brands and store concepts. Further, the strong balance sheet saw them easily able to maintain their attractive, fully-franked dividend.

While they are facing some near-term headwinds – as are most businesses these days – we think this is one to back on any medium-term view and, at the current share price of \$35.38, trading on a FY17 P/E of 14.1x offers good value. Further, the stock is currently trading on a FY17 gross yield of 6.1%, so you are getting paid pretty well to wait in the meantime.

Overall – looks good to us.



Source: Yahoo!7

Stock: Wealth Defender Equities (ASX: WDE)

One area of the market that is seeing increased investor interest is the Listed Investment Company or LIC space. Basically, these are listed stocks whose underlying assets are portfolios of other listed companies. There have been an increasing number of LICs launched in recent years, as many investors regard them as more convenient than a traditional unit trust structure. This is because they can be bought on market just like any other stock – i.e. no forms to fill out – and give a diversified exposure.

One LIC that we can unreservedly say we like is Wealth Defender Equities (ASX: WDE), the LIC that Perennial Value manages. WDE was launched in May 2015, raising \$126 million.

The objective of Wealth Defender Equities is to outperform the S&PASX300 Accumulation Index by investing in a diversified portfolio of Australian shares and using protection strategies to dynamically protect the portfolio through market cycles, thereby reducing the magnitude of significant negative returns in falling equity markets.

Or put more simply, it aims to allow investors to gain exposure the upside of equity markets i.e. long-term capital growth and fully-franked dividend income, while reducing some of the downside risk.

The core of Wealth Defender Equities is a portfolio of Australian shares managed by Perennial Value in largely the same proven, moderate value style that we employ in the Perennial Value Australian Shares Trust. This trust has outperformed the market in 12 of the last 16 years financial years, delivering outperformance of 3.0% p.a. We then use a portfolio of derivatives to cost-effectively manage the downside risk, with the aim of cushioning the portfolio in the event of sharp, significant market declines. The aim is to allow investors to participate in the stock market with a greater “sleep at night” factor.

Since listing, there have been two sharp market declines, August 2015 and January 2016, and in both cases the protection kicked in and offset a significant proportion of the market decline.

One characteristic of LICs is that, for reasons of supply and demand, their share prices often trade a discount or a premium to the net asset value (also known as NTA) of the underlying portfolio. When a LIC is trading at a discount to its NTA, this presents an opportunity for

investors to buy the underlying portfolio for less than it is worth – the very definition of a good value investment. The investor then not only gets the benefit of the expected long-term return of the underlying portfolio, but also the additional upside should the discount to NTA narrow or close (or even move to a premium).

At the last release on the 9th of September, Wealth Defender Equities had a pre-tax NTA of 88.7 cents per share. Compared to the share price of 76.0 cents, this represents a discount of 14% to the value of the underlying stock portfolio.

So overall, an investment in Wealth Defender Equities provides:

Exposure to a portfolio of quality Australian value stocks;

With the additional benefit of reduced downside risk;

All able to be purchased at a significant discount to underlying value.



Source: Yahoo!7

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