Perennial Growth Management

Perennial Socially Responsive Shares Trust

Monthly Report
31 August 2014

	Month	Quarter	FYTD	1 year	2 years	3 years	5 years
	%	%	%	%	% p.a.	% p.a.	% p.a.
Perennial Socially Responsive Shares Trust*	0.6	4.6	4.6	16.4	19.8	15.4	8.8
S&P/ASX 300 Accumulation Index	0.6	3.6	5.0	14.1	18.8	14.0	9.1
Value Added (Detracted)	**0.0**	**1.0**	**-0.4**	**2.3**	**1.0**	**1.4**	**-0.3**
Net Performance	0.6	4.3	4.5	15.4	18.8	14.3	7.8

* 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 31 August 2014):
AUD51.2 million

Income distribution frequency:
Half yearly

Team FUM (as at 31 August 2014):
AUD2.5 billion

Minimum initial investment:
$25,000

Trust inception date:
December 2001

APIR code:
IOF0117AU

- **The Trust performed in line with the S&P/ASX300 Accumulation Index in August**
- **Reporting season was the focus in August.**
- **Contributors to performance for the month were BHP Billiton (down 5.2%, Not Held, Restricted), Mermaid Marine (up 14.0%) and CSL (up 8.9%).**

Trust performance overview

The Perennial Socially Responsive Shares Trust (the Trust) performed in line with the S&P/ASX300 Accumulation Index (the Index) in August, with the Trust climbing 0.6% and the Index rising 0.6% for the month. The Trust has experienced a solid twelve months to the end of August, outperforming by 2.3% and delivering investors a return of 16.5%, compared to the Index which returned 14.2%.

In the month of August, healthcare (up 6.6%) was the standout sector while the mining stocks gave back some of their recent gains dragging down the materials sector (down 3.7%). The telco sector (up 4.3%) continued its recent strong performance. The energy sector (up 3.9%) also beat the index. Notable sectors which were weaker included the banks (down 0.2%) and consumer staples (down 0.4%)

Reporting season was the focus in August, with the most significant theme being more companies beating forecasts than those missing forecasts. It should be noted that market expectations had been moderating as the post May budget malaise and weaker outlook for the Chinese economy were being factored in. The reporting season saw many companies introducing cost reductions as a major driver of earnings growth and companies taking specific provisions below the line to aid future cost out exercises. Companies with increasing dividend or capital returns were rewarded.

The greatest contributor to performance for the month was BHP Billiton (down 5.2%, Not Held, Restricted). As the Trust does not hold shares in this company, the falling BHP Billiton price created a positive contribution to the Trust's return relative to the Index. The main cause of BHP's share price weakness was the falling iron ore price which resumed its year-long downward trend in August. At month end, spot iron ore prices reached the August 2012 low and due to this we estimate that consensus earnings and cash flow projections for all iron ore companies will need to be downgraded. In our opinion the market's expectations of capital return to shareholders next year will also prove unlikely.

Mermaid Marine (up 14.0%) also contributed to performance. In early May this year Mermaid announced plans to acquire the assets of Jaya Holdings, a Singaporean based Vessel Company. This move was transformational for the group as the transaction expands the company's presence in the Asian region at a time when their local clients are reducing their level of work as they transition from construction to production activities. The weakness in the share price of Mermaid prior to this month was a result of the equity capital raising used to fund the acquisition and the market consensus not fully appreciating the strategic importance of the move. With the reporting of the full year result and a growing understanding of the potential for the new business, confidence has been restored in the company.

The Trust also benefitted from its holding in CSL (up 8.9%). Leading into the CSL financial result, the market was concerned due to previously reported profit warnings from two European competitors. Contrary to the market's expectations, CSL's figures showed that it is outperforming its peers in sales in its key product areas, notably IVIG (+12%), Albumin (+16%) and Specialty Products (+18%) while simultaneously expanding margins. On the back of this news, CSL rallied 17% off its intra-month lows. CSL committed to undertake another $950m share buyback after completion of a debt raising. Importantly, CSL management's outlook commentary was strong, with the company guiding to 12% NPAT growth and stronger growth in EPS due to the ongoing share buybacks. We remain attracted to CSL's above-industry growth rates, prospective R&D pipeline and strong ROIC.

The main negative contributor in August was JB Hi-FI (down 13.8%) following its FY14 results. JB Hi-Fi announced NPAT increased 10%, in line with company guidance, however like for like sales in July declined 5.5% predominately due to weakness in the tablet category. This weaker start to the year led to a relatively muted FY15 sales growth guidance which resulted in share price weakness after the result announcement. Whilst disappointed with the weaker start to the year and the sales guidance, we still see several growth drivers for JB Hi-Fi including both the JB Home appliance and the Commercial businesses which complement the ongoing rollout of the core electronics store format. In FY15 we remain optimistic that the release of the iPhone6 will drive store traffic and also that JB Hi-Fi won't experience the same inventory shortage in game consoles that it experienced at Christmas this year resulting in restricted sales in this category. Based on our estimates the valuation is undemanding with greater than 25% valuation upside, supported by a strong balance and excellent cash flow generation.

WorleyParsons (down 8.7%) fell after reporting a result that was at the bottom end of the guidance range. Margin performance in the second half of the year was encouraging driven by an aggressive cost out program (2,200 overhead positions were eliminated during the year) and strong cash generation was also a highlight. Investors were concerned by management's commentary around the flat outlook for Hydrocarbons capital expenditure which is the key driver of WorleyParson's revenues. We believe that the company is well positioned to resume earnings growth in FY15 due to a solid period of contract wins and a significantly more efficient cost structure. Worley continues to have strong cash generation and we believe the current share price undervalues the long term future of the company's globally successful business model.

Mayne Pharma (down 9.2%) also detracted from performance. The company reported a full year result which was ahead of market expectations. However it appeared that the market focussed on lower revenues which were brought about by negative sales growth of one of the company's key drugs. The key issue at hand was that the company's US distributor of this product, Warner Chilcott, was taken over by Actavis late last year and the subsequent restructuring has disrupted sales performance. Mayne Pharma management expect sales to normalise later on this year and have highlighted the importance of the company's product diversification and insourcing of distribution strategies as a means to prevent similar outcomes in the future. To this end the company has 17 products pending approval with the Food and Drug Administration (FDA) in the USA. As each of these drugs move through the approval process we see significant revenue growth coming through over the medium term.

Market overview

The global equity markets were stronger in August with the MSCI World Index up 2%. The US equity market was the standout with the S&P 500 gaining 3.8%. The Australian market showed a modest gain in August of 0.6%. The weaker mining sector weighed on the domestic market over the month. The major European markets were up over the month despite weaker economic data as investors focussed on further monetary stimulus from the European Central Bank. European bond markets rallied strongly, with the 10 year Bund reaching a record low yield of 0.9% while the yield on two year paper dropped below zero. The Euro Stoxx 50 rallied 1.8%. Most other regional equity markets were weaker during the month with Hong Kong's Hang Seng (down 0.1%), Japan's Nikkei (down 2.5%) and China's Shanghai Composite (down 1.5 %) all falling.

Within the US, the second quarter GDP data was revised upward by 0.2% to 4.2%. Consumer confidence indicators were strong together with the Purchasing Managers Index which also surprised on the upside. The unemployment rate rose slightly, up 0.1% to 6.2%. An interesting observation was a rise in the participation rate to 62.9%. The participation rate has been in long term down trend a stabilisation of the downtrend could be viewed as a bullish indicator as the general population are encouraged to re-join the workforce. The housing data was stronger with starts rebounding 15.7% in July and housing permits up 8.1%. The housing data has been volatile on a month to month basis however the general trend is positive. Overall the economic data from the US confirms our view that the gradual economic recovery remains on track.

Chinese economic data was weaker after some stabilisation over June/July. The HSBC Manufacturing PMI fell to 50.3 a three month low. The Chinese M2 Money Supply for August moderated at an annual growth rate of 13.5% year on year (14.7% year on year to June). The major economic data that raised serious concern was the loan growth data released by the Peoples Bank of China (PBoC) which showed a collapse in new loans by 45% year on year. The PBoC was quick to point out in the release that there had been an abnormal increase in the June data which partly reversed in July. We will need to see the August data for a clearer trend. Currently, all the evidence points to an ongoing slowdown in the Chinese property market. We remain firmly of the view that this will translate in to weaker end demand for steel and further weakness in the iron ore price.

Domestically, economic data was marginally better in August with the Westpac Consumer Confidence Index rising 3.8% and retail sales rising 0.6% which was above market expectations. The true state of the labour market in Australia was also a dominant theme as the unemployment rate jumped to an unexpected 6.3% while the level of employment was largely unchanged. While the ABS noted that technical changes accounted for a significant proportion of the lift, the RBA's view appears to be that labour market conditions will remain subdued as the economy continues to grow at a sub trend pace. According to the latest Statement on Monetary Policy, the RBA believe the economy will grow at 2.5% over the next 12 months before growth lifts to 3% the year after. Sustained labour market improvement is not expected until 2016.
The Australian Dollar (AUD) increased 0.5% against the USD to 0.9339. The USD was stronger against most major other currencies. The Euro was particularly weak, falling 1.9% against the USD. Concerns over the direction of the European economy and potential for another round of monetary stimulus were the main drivers of Euro weakness.

The concerns over a weakening Chinese economy and increasing supply in bulk commodity markets reasserted themselves in August. The price of iron ore fell 8.1%. Elsewhere in commodity markets, the price of oil (down 2.3%) fell as increasing supply more than offset concerns about ongoing conflict in the Middle East. Base metals were mixed in August with zinc (down 0.8%), aluminium (up 5.5%) and copper (down 1.8%). Despite ongoing unrest in the Middle East and the Ukraine the gold price showed only a modest increase of 0.4% in August to close at US$1287.8/oz.

Top 10 Holdings

Stock name	Trust weight %	Index weight %
National Aust. Bank	7.9	5.9
Commonwealth Bank.	7.3	9.3
ANZ Banking Grp Ltd	7.2	6.5
Westpac Banking Corp	6.7	7.7
CSL Limited	4.8	2.5
QBE Insurance Group	3.3	1.0
Lend Lease Group	3.0	0.5
WorleyParsons Ltd	3.0	0.2
Santos Ltd	2.8	1.0
Insurance Australia	2.6	1.1

Asset Allocation

Sector	Trust weight %	Index weight %
Energy	11.4	6.3
Materials	8.8	16.8
Industrials	9.0	7.1
Consumer Discretionary	2.5	4.1
Consumer Staples	0.8	7.8
Healthcare	10.7	4.9
Financials-x-Real Estate	42.0	37.9
Real Estate	5.6	7.1
Information Technology	0.8	0.8
Telecommunication Services	2.8	5.4
Utilities	2.3	1.7
Cash	3.2	-

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